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INDIAN BUSINESS

VOL. I

Aspects of Organisation & Finance

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By the same Author

INTRODUCTION TO MONEY

INTRODUCTION TO BANKING

INDIAN BUSINESS—VOL. II

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*Dedicated
to the
Sacred Memory
of my
Beloved Father*

PREFACE.

When I joined the Deccan Education Society's College of Commerce at Poona in June 1944, I was entrusted with the work of teaching Business Organisation, a subject though not entirely out of line for a student of Economics, yet not perfectly in line even. Hence I took up the study. But to my surprise I found that although commercial education in this country, particularly in Bombay, has come to assume great importance, there is no book available on the subject, and hence the students as well as the teachers have to depend on foreign stuff imported in this country and not applicable to Indian conditions. Upto now only a few notes by Indian authors exist, mostly written for money making and not for imparting true business education. If the aim of the author had been to make business with the book while omitting altogether the loftier ideal, the purpose has no doubt been well-served. But so far as the advancement of business education is concerned, this labour has been entirely in vain. For, business education does not simply mean the cramming of a few points from the notes and disgorging them in the examination papers. The true business education should interest the student for business. I recollect the remark made by A. J. Sargent: "One of the hardest tasks of the teacher is to instil into the mind of the student the fact that he is being trained *for* business, in the widest sense, but not *in* business, and that it is the training that matters, rather than the memorising of some special groups of facts. . . ." Another thing. Business education to be effective must be practical, must keep in touch with business developments in this country as also abroad. For, business education aimed at producing clerks for business concerns and not at producing entrepreneurs is no business education at all. For, *Kaulinya* or aristocracy of an individual as also

of the nation depends to-day on income, individual and national.

यस्यास्ति वित्तं स नरः कुलीनः

स पण्डितः स श्रुतिमान् गुणज्ञः ।

स एव वक्ता स च दर्शनीयः

सर्वे गुणाः काञ्चनमाश्रयन्ते ॥

In fact this should be the aim of business education.

A few words may now be said regarding the plan of this work. This survey of Indian Business has been planned in three volumes. The first volume is concerned with the organisation and finance of business along with an introductory chapter which considers the meaning and scope of business. The second volume is concerned with commercial organisation in India. The introductory chapter considers the stages of commercial development of India from 16th century onwards and traces how India is marching, slowly but surely, towards a balanced economy. The first part of volume II considers trade organisation, the second part credit agencies in India, the third part insurance and the fourth part transport. The last chapter considers the role of the state in economic development of India. The third volume is concerned with efficiency aspect of business, and the inspiration for adding this volume came from the various Reports of the Balfour Committee appointed in England in the mid-twenties to consider the various aspects of efficiency with a view to suggest measures for their improvement and thereby to increase the competitive efficiency of British industry and trade which had declined since the years of the first great war. It is true that our problem is entirely different; yet we are also passing through an important period in the economic development of our country and on the decisions we arrive at and the steps we take now that our future economic destiny depends. To-day, the best thoughts of the nation are diverted towards devising the ways and means for economic progress. Everyone conscious is thinking of planning. But planning can only be effective if we take a stock of the existing situation—on what foundation we are going to build up the economy of the future. The third

volume is therefore an effort at stock-taking of our business situation and expects to provide inspiration for the business leader of the future. But my purpose is not mere stock-taking. I have also tried to indicate the weak spots in our economy, with suggestions, as far as practicable, for their removal. The introductory chapter of Volume III considers Efficiency as a factor in Business. Then it considers cost and efficiency, management and efficiency, size and efficiency, rationalisation and efficiency, labour and efficiency, wages and efficiency, industrial peace and efficiency, welfare and efficiency and lastly, marketing and efficiency. One chapter is devoted to scientific research, industrial mobility, industrial art, business cycle and statistics and business profits. In this work India has been considered as a whole and not after partition.

The difficulty in compiling such an extensive work has been a real one. There is no easily-available material so far as this country is concerned. Whatever scanty material is available in the pages of the Tariff Board Reports, various year books, statistics published by some business associations, the annual speeches of the chairmen of the boards of directors of various business concerns and their balance-sheets has been brought together and analysed with acknowledgement in proper places. Some of the official enquiries have been of considerable help. Besides, the standard works on the subject by foreign authors have been consulted for comparative analyses and studies. In spite of all these efforts, I am quite conscious that a work of this sort cannot be all-comprehensive and up-to-date and has many weaknesses. Besides, those who will seek in these volumes the standard of economic development which has been attained in some of the western countries are sure to be disappointed. For, in comparative equations, we are one hundred years behind these countries and hence they should judge the present situation with a century-old outlook and devise ways and means for its rapid development.

Finally, I must thank the editorial boards of the *Indian Journal of Economics* (Allahabad University), the *Indian Co-operative Review* (Madras) and the *South Indian Journal of Economics* (Guntur) for publishing parts of this work in the form of articles. I must also thank my colleague and friend, Professor D. G. Karve, Principal of the College of Commerce,

Poona, in entrusting me with the work of teaching this subject in his college, but for which it would never have been planned. And lastly, I thank Mr. Puranik, the Librarian of the same college, for supplying me with necessary books from his library as also from the Wadia and Servants of India Society Libraries and my wife, Mrs. Kamala Lalwani, for helping me all through in taking down notes and in various other ways, but for which it would not have been possible for me to complete the work so early.

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K. L.

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CHAPTER I

INTRODUCTION

Definition and Scope

The word 'business' is wide as well as narrow in its connotation. In its narrow sense, it means purchase and sale of a commodity and/or service with a money-earning motive. In fact, it is this profit motive that is guiding all business transactions in all societies, both ancient and modern. But in broad sense, the word includes a variety of things, which, for the sake of convenience, we may place under two heads—business, productive and distributive, and business proper and aids to business.

So far as the first variety is concerned, its two sub-types, though nowadays regarded as equally productive, were not regarded with the same importance in days gone by, while the word 'productive' was also used in a very narrow and restricted sense. Thus according to the Mercantilist doctrine, productivity is to be determined according as whether the particular work is leading to favourable balance of trade or not. In the writings of the Physiocrats, land and bounty of nature have figured most. With Adam Smith, the conception slightly yielded its narrowness but it still excluded works, which did not bring forth 'vendible' commodities, from 'productive' work. Service, which is not a vendible commodity, has thus no place in the list of productive work, according to this definition. Today, however, we are giving up the Smithian distinction between productive and unproductive work, unless, of course, the work is totally useless from social or communal standpoint. The distinction has come to be regarded as one of degree and not of kind.

Turning to the second sub-type of the first variety, it may be mentioned that the distributive aspect has long been either neglected or regarded with contempt by both the spiritualism of the East and the philosophy of the West. So far as the East was concerned, it was quite natural and keeping in with

their ideal of plain living and high thinking. So also with the West. Thus Aristotle makes a distinction between natural and non-natural occupations, the latter's object being the making of money for its own sake, for commerce was regarded as the means of felching something from neighbour. Agriculture as a means of living received the blessing of all. Husbandry and stock raising followed suit. But exchange, in any other way, whether of commodity, money or service, was greatly regarded with contempt. This contemptuous attitude towards the distributive aspect of business found expression not only in the writings of the master minds of the age but also in the social rank given to businessmen. Thus in India they occupied the third place, immediately before the non-Aryans but always ranking after the scholarly class and warrior races. In Muslim period also the business community had to undergo certain restrictions. Thus at the time of the Mughals, they were debarred from exposing their riches. Luxury became more or less a monopoly of the nobility. The 18th century saw a remarkable change in the attitude towards the business community, both in the West and in the East. With the growing importance of the economic aspect of man's life, which came to supersede the other aspects, a new aristocracy composed of city merchants and traders emerged. India was no exception to this. It is true that in India the obstacles in the way of the rise of this new aristocracy were very many; for, various imposts, exactions and fines were levied on the new aristocracy. But the rise and progress was as sure as it was certain. Further impetus was given by the discovery of the use of many articles which subsequently figured most in the inland and foreign trade. With the advancement of civilisation, our wants multiplied, and the natural impulse of man for the satisfaction of his wants led to the uses of sundry commodities and to the different uses of the same commodity. Revolution in the means of transport gave further impetus to distributive aspect of business and the development of both internal and foreign trade and especially wholesale and lengthy trade operations gradually built up a strong and competent mercantilist community.

Aids to business should also be regarded as a part of business. Business today has lost its primitive simplicity. It

is no longer mere purchase and sale; it is purchase and sale with efficiency and economy of effort. This has brought to the forefront banking, insurance, transport and a lot of other things which on the one hand have led to division of labour and on the other the attainment of maximum possible efficiency, thereby facilitating the earning of profit by the individual businessman and the prosperity of the totality of the business community.

Thus we see that business includes so many things in its widest aspect. It not only includes production, but also distribution of the produced commodity and also the different agencies which are aiding both. We have reached a stage in the development of the economic life at which we cannot say that this or that aspect of business is of greater or less importance. For, they are all equally important and inefficiency in one will have a crippling effect on the entire economic structure.

The scope of business does not end there. Politics is a factor which today is exercising a great influence on business. In present day economy, it is influencing not only inland business but also foreign business. Where inland business is undeveloped, the administration has to come forward with a plan for the systematic exploitation of existing resources, some of which may be, and in fact are, scarce, and thereby to progress towards industrialism. Russia is the best example of this type. In others the administration is simply to reorganise an already developed economy, either with more state intervention as in the U. S. A. under the New Deal or with less state intervention as in England since 1924. State assistance to foreign business has taken various shapes, beginning with the raising of tariff walls to the direct state intervention in certain fields. Control of money, banking and finance has not been the same in all countries but have varied in order to suit the different requirements of various economies; but hands-off-business policy is unthinkable. *Laissezfaire* was a misnomer yesterday; it is equally a misnomer, nay, a greater one, today. Mercantilism, in one form or other, in restricted or wide sense, is the underlying spirit of world business.

The ethics of business is expressed in the well-known dictum, 'Honesty is the best policy.' It is well known that the

entire business structure of today stands on the institution of credit and credit implies confidence. One can earn a huge wealth by dishonouring one promise; but this he can do only once and for that he stakes every thing. Business reputation, like a good name, is the result of continuous practice of honesty for years, or generations, together. It is difficult to earn but easy to waste and squander; and so long as it is not earned, it is the aim of every true businessman to earn it and once earned, it is his look-out to preserve. What strikes me most in Indian business is its high sense of morality. I do not mean to say that morality is lacking among non-Indian communities in business. But the peculiarity of Indian business is that it is not based on implied force. Word is word and once it is given, an Indian businessman will honour it at all costs. 'Word' in indigenous transactions is scarcely backed by written and duly signed and stamped documents, and hardly given before any witness. Yet the wonder is that few or no disputes will be seen arising as a result of broken promises. This characteristic of business is peculiarly Indian and has a long tradition. In fact, it is this particular feature of Indian business that attracted the attention of foreign travellers to India, and particularly of Tavernier, whose accounts are the standing proofs of the same; and even today, under the impact of western business practice which is rapidly entering the borders of India, the traces of the indigenous practice of transacting business simply on words, though gradually disappearing, has not yet become non-existent.

And finally we must mention of psychology which comes within the range of study by business. The subject is as much complicated as it is abstract. But that it is important and cannot be neglected in view of its all-pervasiveness is equally clear. In production, which takes place in anticipation of demand,—not only local, but also national and international,—the need for business forecasting is quite apparent. In distribution, the subject includes a study of the nature and extent of demand in each market so that scientific distribution of produced goods may take place thereby minimising the risk of deadstock. There is still another aspect, which is concerned with the potential demand. The spread of the use of tea is an illustration in point. The need for the conversion of

potential demand into a real one necessitates the study of the psychological weakness of the would-be consumers and advertising is the medium for making this exploitation-motive of the producer and/or distributor effective.

Another factor coming within the range of business psychology is expectation—expectation not of existing and potential demands but expectation of profit. It is peculiar that so important a subject as expectation was long neglected by writers in Economics though, of course, not by the business community. In recent economic literature it is getting its place. In fact, expectation of earning plays a part of greater importance than actual profit earned. For, while the extent of actual profit is not predetermined, it is the expectation of profit that induces a businessman to come forward and that to a great extent determines the volume of business. It is true that cost factors play an important role in the determination of expectation; but if the expectation is rosy, even the cost factors cannot deter advance. Cost factors are known to him more or less; but the producer will have to anticipate what he can get from the consumers in exchange for his goods. For, the greater the difference between sale proceeds and total costs, the greater the profit that he can derive and the greater will be the business incentive. It must, of course, be borne in mind that the aforesaid difference cannot be an arbitrary amount over a period unless the particular line is in monopolistic control. For, otherwise, too big a difference between sale proceeds and costs of production will attract the flow of capital in a particular channel and, that too, so long as the fabulous profits do not evaporate. It must not be taken to mean that the flow is unobstructed, for, devices like stock watering are sufficient inducements for the concealment of big profits in present day business. Yet that the natural tendency is there cannot be denied for the formulation of general principle.

The important part played by expectation is now realised. It is true that this dependence on expectation involves the shouldering of risk. But this the businessman must be prepared to undertake, if he wants to carry on production by processes which take time. He must be ready to face unforeseen changes reacting unfavourably on his business expectations

and in general it may be said that the lesser these changes, the greater the accuracy of expectation and the greater will be the profit derived from business. Or in other words, the more successful businessman is he whose expectations are more accurate or less inaccurate, who knows the tactics of averting unforeseen dangers or preventing altogether their appearance by the adoption of special devices suited for the purpose, and who has sufficient financial strength to meet the danger when it is inevitable.

In current economic literature a distinction has been drawn between short-term expectation and long-term expectation. Thus in the words of *General Theory of Employment, Interest and Money*, short-term expectation "is concerned with the price which a manufacturer can expect to get for his 'finished' output at the time when he commits himself to starting the process which will produce it"; the long-term expectation "is concerned with what the entrepreneur can hope to earn in the shape of future returns if he purchases—or, perhaps, manufactures— 'finished' output as an addition to his capital equipment." The distinction though clear-cut in literature is not so in practical field. For there is a process of continuity between the two and even then they are always changing. Modifications of expectations are to be made in accordance with the results achieved. This necessitates an acquisitive brain. Rigidity or orthodoxy in the field of business has been the fruitful cause of the collapse of many a successful concerns.

These expectations exert their influence on the business field over a period of time, though in abnormal situations of trade boom and slump jerks in expectation are not rare. It is true that changes in psychological conditions are not the only causes of boom and slump; but at the same time, we cannot deny the part played by them. But in general the effects are continuous. Whether in the field of production or in the field of distribution, any change of expectation cannot lead all on a sudden to an expansion or contraction of business. Abandonment or contraction of work is a more time-consuming process than even an expansion. In matters of expansion some time must elapse before the necessary preparation is made; in matters of contraction, unfavourable expectation is

supplemented by hesitation, which makes the process all the more continuous. For, the catastrophe overtaking business may be rather short-lived and the business may revive. This makes the process slow. But even this slow process may not be devoid of some oscillation. For, before the long period expectation has worked itself out, the temporary impetus may lead to over expansion unwarranted by the long period expectation. In such a case there will be movement backward to the position which is relevant to the new expectation. The opposite course is equally true in case of contraction. And again this takes place not only when the volume of business expands and contracts but also when the existing volume of business changes its course according to the changes in the nature of demand.

Thus the business situation at any moment is not the resultant of the decision taken once but is the result of the sum total of decisions taken up to that time along with the most immediate one. The existing state of business along with its capital equipment in the field of production and distributive machinery in the field of distribution is the result of past decisions, which is simply modified this way or that according to the decisions taken on the basis of current expectation. Now, it may be asked, what are these factors on which expectation depends? The answer is obvious. . Two factors seem to be of importance, viz., the current facts which in the field of production depend on "the existing stock of various types of capital-assets and of capital-assets in general and the strength of the existing consumers' demand for goods which require for their efficient production a relatively larger assistance from capital" and in the field of distribution on the stock in hand, the nature and extent of the distributive machinery and the goodwill that they have been able to attract and so many other factors; and the business forecasts which in the field of production depend on "future changes in the type and quantity of the stock of capital-assets and in the tastes of the consumer, the strength of effective demand from time to time during the life of the investment under consideration and the changes in the wage-unit in terms of money which may occur during its life," and in the field of distribution on the stock-in-hand, nature and extent of the market and effec-

tive demand therein and also goodwill that it has been able to attract.

Keynes has devoted some thought to the consideration of the state of Long-term Expectation and the object of the analysis is to "consider in more detail some of the factors which determine the prospective yield of an asset." But the field explored is extremely narrow and he has concentrated his attention on "the price of shares," the fluctuations in whose prices are "highly significant daily, even hourly, revaluations of existing investments carried out in practice." Thus he is attaching more importance, so to speak, to "the average expectation of those who deal on the Stock Exchange as revealed in the price of shares, rather than by the genuine expectations of the professional entrepreneur." But this sort of analysis does not give a true picture. It is not the investors on the Stock Exchange that take the decision as regards investment; it is the promoter of the concern. The promoter, who has the natural qualities of head for the successful floatation of a new enterprise, takes all the decisions before he jumps into the enterprise. It is true that the minimum subscription clause will have to be fulfilled before a concern starts operation; but since here the capital is limited, it may come, and generally does so, from a restricted circle. The public issue of shares may be offered at a subsequent date, when all other circumstances are favourable. Even when some of these other circumstances are not favourable, e.g., when the rate of interest is high, it need not deter the public issue of shares or debentures if the expectation of opportunity is too great to be missed. Sometimes shares of a particular concern are subscribed to not because it is paying high dividend at the time of purchase but because of the sound personnel of the Board of Directors or because the concern is under the managing agency of a reputed firm. Thus the rate of interest plays a comparatively minor, though not altogether negligible, role in the determination of the volume of business. It is rather peculiar to find that in recent economic literature so much importance has been attached to the rate of interest as one of the determinants of the yield from investment, and therefore, of the volume of investment.

To consider the matter from another standpoint, the rate of interest at which money may be available and price at which

the shares may be sold are not the same for different concerns, nor are they same for the same concern over a period of time. Therefore to speak of the average yield of the totality of investment being equal to the rate of interest or to make the latter as the determinant of the former is to exaggerate matters. Even in the same concern, the variation in the rate of interest and in the price of securities over a period of time should not be considered as a reflection of the variation in yield. When rate of interest for a particular concern goes up, it should not be taken to mean that the concern is yielding high profit. This increase in the rate of interest comes, of course, owing to a rise in the demand for capital. But this does not mean that the increased demand for capital is always due to the expansion of business as a result of the stimulus of high yield. Even a poor concern may be offering high rate of interest not because it is earning high profit but because it needs capital at all costs and an offer of high rate of interest may prove sufficiently attractive to the would-be investors. And in a well-established concern, the increased demand for capital may come from factors like increased new issues, sale of existing securities to raise money etc. A rational method of analysis is to consider each individual concern on its own merit instead of taking the total volume of business into consideration. Equilibrium for the whole system is a misnomer, since there may exist simultaneously so many oscillations for an individual concern or a few concerns.

The true relation between the rate of interest and the yield from a particular concern is not inverse but may be reverse. Concerns with fair and steady dividend payments can attract capital at low rate of interest. Just the reverse with concerns offering fluctuating and uncertain dividends. The rate of interest is high not because the yield from the concern is low but because the latter is uncertain. The rate of interest is low not because the concern is giving more or less dividends but a steady one. That shows that the public have confidence in its soundness. Therefore it is the confidence of the public in the soundness of a concern that determines the price that they will quote for the money they are going to part with and not so much the actual yield from a public concern.

In case of borrowing, the rate of interest is predetermined.

irrespective of subsequent yield and sometimes the rate of interest is so high that for years together no payment of dividend is made on ordinary shares. High interest is offered on bonds or debentures not because the concern can but because it must. Thus when we speak of saving and investment in the consideration of economic theory, we think that enough has been said. But it is just the beginning of the story. For, after a decision to save is arrived at, the next step is to consider whether the saver wants to be a proprietor or a creditor, the former with uncertainty as to earning, both for high and nil and the latter with a fixed income but no share in excess profit. The next step for him will be the nature of the business in which he is going to invest; for, different concerns do not give the same rate of interest on debentures nor the same dividend on shares. It all depends on the soundness of the concern, the nature of the policy pursued by the Directors in these matters and the availability or otherwise of capital so far as the concern goes. This analysis all the more strengthens our previous conclusion that it is wrong to speak of a rate of interest for the total investment of society but each concern must be considered on its own merit.

Thus in the case of a sound concern,—and if the concern be new, then if the concern has a Board of Directors consisting of reputed businessmen—capital will be forthcoming not because the concern is offering high dividend or high interest rate but because of two psychological factors, viz., faith in the soundness of the concern and safety of the investment and expectation of steady and fair income, if not immediately, at some future date.

The volume of investment considered as a whole is not the result, under existing economy, of any prior calculation, but the result of a process of trial and error. The promoters expect to earn profit in the particular line but their expectation may dash against some submerged rock. In the language of economics, the firm has proved submarginal and is forced out by competition from marginal and supermarginal firms. The concern has failed not simply because the rate of interest was disproportionate to the yield; for the matter may be the other way round. At first sight the rate of interest appears to be of prime importance because it is out of the funds obtained that the remunerations of different factors are given; but their cost

can be lessened if the cost of all other factors is equally less. Efficiency of the business depends not simply on a particular factor, but on each and every factor, because it is after all the result of co-operation among them.

Business and Economics

The science of Economics which in its present form started its career with Smith has gone very far; but yet it is peculiar that economic theory has nothing to do with economic and business practice. The economists live in a world which is totally different from the world in which the plain man lives and works, spends and saves; nay, each economist has a world of his own which in some respect or other may be different from the world envisaged by his fellow economists. But one thing is common in all of them, viz., that they are seldom concerned with the world as it is. The recent trends in the study of Dynamic Economics do not seem to be sufficiently dynamic, and in some cases is all the more abstract. The result is that a study of Economics is not enough for an understanding of Business; Business is to be studied from different angle of vision. There is another respect in which Economics differs from Business. In Economics, we do not study merely wealth, but the economic life of the common man with a view to the attainment of maximum welfare for the entire community. In Business the object is not so comprehensive. Since its object is to make profit, the businessman will take to any line, no matter whether the use of goods produced in that particular line is socially beneficial or not. There is no difference of opinion that wine or opium is injurious; yet the business world has not been able to abolish the trade in these, although considerations of welfare should do it. Thus Economics, at least Welfare Economics, is less economic and more ethical.

The theories of Economics are not enough to explain practice; sometimes they give a contrary explanation. Take the case of taxation and price. The practical businessman suggests that in fixing his prices, a trader puts on to his costs a margin of profits for himself and of course it is his profit that is subject to direct income tax; and if he wants to get sufficient reward for his exertions, he must put on an addition to his price suffi-

cient to cover profit to the government and profit to himself. Thus the association of the British Chamber of Commerce pronounced as follows before the *Committee on National Debt and Taxation*: Although theoretically income tax is levied on profits, when a trader endeavours to ascertain his costs with a view to fixing prices, he often takes into account, at least indirectly, the amount of income tax he will have to pay, and if the market conditions permit, fixes his prices at such a level as would yield to him the minimum net income which he desires to obtain or actually needs. Some people go so far as to declare that income tax on wages and salaries is added to prices, since employers have to pay a higher remuneration on account of the tax and the tax therefore enters into costs. And what about the theory? Professor Pigou points out that income tax is assessed on profits resulting from trade and industry and if people are already charging the prices that yield them the best profit, the removal by the state of a portion of profit will not tempt them to fix prices differently. This sort of argument may be correct when the levy is a new one on an already existing trade in which the competition is so keen that no increase in prices can be effected so as to make the levy a part of cost. Under conditions of monopoly or quasi-monopoly which has gone so far as to affect even retail trade or imperfect competition, which characterises present-day industrialism, there is no difficulty in increasing the price in proportion to the levy. That it actually does happen is our everyday experience and whenever a proposal is put forward for any increase in tax rate or for the imposition of a new levy, the supply is generally withheld with a view to charging more price, and sometimes the price goes up even at a mere proposal for levy, though the levy has not yet been imposed.

The question was considered in greater detail by the *Colwyn Committee on National Debt and Taxation*. The Committee's conclusions are similar to those of the other theoretical economists, viz., that "the broad economic argument is true over practically the whole field and for practically the whole of the time, any exceptions being local or temporary and insufficient to invalidate it." But the line of their argument is faulty and hence the conclusion one-sided and partial. When a tax is imposed, the monopolist will raise the price. The rise is not

generally too high; for whatever the rate of the tax, the amount per unit is not enormous and the monopolist finds it quite easy to convince his customers as to the justification for increase in price. And so far as free competition is concerned, it is one of theoretical interest, for in actual world there is no such thing as either free or competition. The joint stock concerns have of course created some confusion in understanding; for as the Committee points out that "so far as a company distributes its profits, it recoups itself by deduction of tax from its shareholders, in the fluctuation of whose individual liability it is not interested." It is a well known practice among joint stock concerns to maintain the rate of dividend payment steady; for, a fluctuation in this tells unfavourably on the price of shares. Besides, the amount paid as dividend comes as much out of sale proceeds as the amount paid in taxation and some of the concerns go so far as to show in their balance sheet an item, viz., "reserve for taxation." This in itself is a sufficient indication that except in exceptional cases, sufficient effort is made to include taxes in costs and in most cases the effort is successful.

There is another reason for which a study of Economics differs from the study of Business. This lies in the over-simplification of economic theories. Let us take the case of price determination. In so far as Economics and Business are concerned with "the study of market processes," they are tackling the same problem. But the task of economist ends with an analysis of the apparatus of demand and supply, an equilibrium analysis, as it is known. But a ~~calm~~ consideration will show that it is more an analysis of price fluctuations than one of price determination. When demand increases, prices go up and just the reverse when demand goes down. The relation of supply to the position of equilibrium is just the reverse; for with an increase in supply prices will go down and with a decrease, they will go up. Equilibrium is a position at which these two forces of demand and supply, the two blades of a pair of scissors, equilibrate. But the businessman is not satisfied. Demand and supply are not determining price; they are simply forces that may bring about oscillation. What then determines price? The businessman knows it well. We have already said, business has productive aspect, distributive

aspect and there are certain aids to business. The businessman will consider each and every item of cost plus profit to government and profit to himself and thus fix the price. Apparently simple, the procedure of price fixation is a difficult task and requires the best thoughts of the businessman.

To whatever economic theory we turn, we find that each and every one of them is concerned with, and conducting an enquiry in, "the framework of its appropriate market or markets." The theories of money and credit, those of distribution of income, of saving and investment, of trade boom and depression,—all are concerned with the analysis of the same sort of problem—namely, fluctuation in prices. For none of these has anything to do with price determination but with price fluctuation. If the volume of money and credit be doubled, the theoreticians will say that the price will go up twice as high as it previously had been. If there is a more even distribution of income, prices may be more or less steady. If savings and investments are equal, the economy may be stable. And so on and so forth. But none of them considers the factors which will determine price, and at what level. For leaving aside the four factors of which the economists speak, there are so many other economic and non-economic factors which exercise not a very negligible influence on prices. For instance, the factors of distribution are entirely neglected in Economics, though they are as much important as factors of production. Besides, the non-economic factors, which though not coming within the range of economic considerations, yet enter into cost and influence price.

For long the consideration of price fluctuation was restricted to a competitive free economy, with the result that even the analysis of price fluctuation lost all touches of reality. In recent years however this gross error in economic analysis has come to be detected and some attention has been given in this direction. The formulation of the concepts of "imperfect competition" and "monopolistic competition" are cases in point. But they by no means are exhaustive; for imperfections and monopolisation in competition do not take the same form under all economies, but are varied and exert diverse influence on price mechanism in different markets.

There is still another respect in which the present-day Eco-

nomics has failed when considered from the standpoint of business. Take, for instance, the case of wage determination. Here, as in other branches of economic analysis, there is as yet no unanimity among economists. However, it must be admitted that the theories of marginal productivity and standard of living in one shape or another have the greatest following. So far as the marginal productivity theory goes, it is based on certain assumption the validity of which determines the validity of entire subsequent structure. The more important of these assumptions are that there is free competition among the producers who are demanding the services of factors of production and that there is perfect, or a certain degree of, mobility of the factors of production, including labour, both of which are not to be found in actuality. However, on the basis of these assumptions, it is argued that free competition will tend to bring about an equality of incomes for similar factors of production in every industry. "As between persons who are not exactly similar, fairness in the above sense implies real wages proportioned to 'efficiency'; the efficiency of a worker being measured by his net product conceived as marginal, multiplied by the price of that product." The argument appears to be quite reasonable. But under a time-wage system where wages are determined not according to the realised productivity of the worker but according to the anticipated productivity, that anticipation too being made by the employers under conditions where there is no sufficient mobility for labour and where the labourers are not organised sufficiently so as to bargain on a footing of equality, the so-called marginal productivity becomes no productivity at all. One is at once reminded of Marx's remark that the economists are the mouthpiece of capitalist producers always singing in justification of the system they have developed on the basis of exploitation. How far the Marxian contention is correct is a matter beyond the scope of the present volume, but that the wage system was unjust and unjustifiable is sufficiently testified to by the subsequent adoption of piece wages in many concerns and the theoretical support given to a system of piece wage scales controlled by collective bargaining. Just observe that even the piece wages have not been deemed sufficient but have been supplemented by collective bargaining. How far collective bargaining may be of any use for the pro-

tection of labour in countries where labour is not yet properly organised is a different matter. But the cautiousness of the economists is rather remarkable. To take a concrete case, it was revealed in the enquiry by the *Bombay Textile Labour Enquiry Committee* that "the survey of wages in the cotton textile industry in this province... indicates the very wide disparities that exist between the earnings of workers in the different centres of the industry and in different occupations in the same centre. In most centres there are similar variations in the scale of payments from unit to unit. The continuance of these disparities is mainly due to the lack of cohesion among the employers and of bargaining strength among the employees." An idea of disparity can be had from the following table regarding the wages in Cawnpore textile mills.

Table showing disparity in wages in Cawnpore:
(Per month of 26 working days.)

		Rs. A. P.	Rs. A. P.
Roving Tenters	...	13 15 0 to 37 2 8	
Ring Siders	...	12 6 0 to 23 10 0	
Grey Winders (old type)	...	10 5 0 to 27 0 6	
Two-loom Weavers	...	22 14 0 to 39 12 0	

The variation of productivity for the same sort of worker in different mills, nay, in the same mill, cannot be so wide as indicated above. Any method of averaging the highest and the lowest rates to find out the fair wage level would be too arbitrary to need consideration. "If in a country like India where economic conditions resemble very much those envisaged by the classical writers, this disparity between theory and practice makes one sceptical regarding the validity of economic analysis in more advanced countries where obstructions from the standpoint of the employers, of the workers and of the state hamper at every step the working of a free economy." (Gadgil, D. R.)

Turning for a moment to standard of living, it will be found that wages paid have nothing to do with it. It is apparent that the injustice of the piece wages scale under conditions of 'efficiency' system of working lies in the fact that the contribution made by labour is becoming less and less. Thus since owing to the adoption of labour-saving devices, the contribution of labour per unit of product decreases, the price that he

will get will naturally come down, thereby telling adversely on his standard of living. That it is not merely a matter of argument but a grim reality is testified to by the growing demand for minimum wage legislation and the state intervention in this respect. In India the demand for minimum wage legislation was made long ago, but apart from the voluntary adoption of minimum wages on the recommendation of certain trade associations, nothing has so far been done by the state. The appalling condition of the workers was revealed at the time of the enquiry made by the *Bombay Textile Labour Enquiry Committee*, which will be considered in its proper place. But suffice it to say here that what is true of the textile industry is all the more true of any other industry in this country and the concept of standard of living determining wages is nothing but a misnomer.

Finally we must consider one more theory in order to see that economists do not agree among themselves, thereby making it impossible for the practical businessman to listen to the former's advice. Take the theories of profits, for instance. Although a consideration of profits is most fundamental not only from the standpoint of individual earner and the corporation, but also from the standpoint of national income and public finance, yet upto this time the economists have not been able to formulate any concept which may be of assistance in practical world. All the discussions on profits upto this time are concerned with finding out some justification for it, but not how it is actually determined. To the economists, profits are the share of the fruits of industry that go to the entrepreneur. According to them, just as rent goes to the landowner, wages to labourer and interest to the capitalist, in the same way, profits are the remuneration of the entrepreneur. Since it is not their duty to determine the exact amount of profit in any particular case, the economists are content to deal only in generalities. But so far as the businessman is concerned and so far as the state is concerned, this sort of short-cut leads nowhere.

The determination of profits for a sole proprietorship is of some importance but their determination causes no great concern. With a corporation, however, the inter-relationship among the participants and with the state necessitates more

exact calculation of profits. The participants are concerned with more and more dividends. For the would-be investors, efficiency is measured in terms of profits earned. So far as the state is concerned, it is interested in taxes and some of the taxes may be measured by profits. Sometimes, for maintaining the integrity of the concern, the state may have passed laws against fabulous dividends and that too requires an accurate calculation of profits. But in this respect the theories of economics are of no help and we must go to an accountant for the calculation of profit. The accountant would at once say that by profit is meant net profit. As such profit is the remainder obtained by subtracting the operating expenses, e.g., cost of materials and labour, manufacturing expenses, selling expenses, departmental expenses, repairs and depreciation, etc., from the sale proceeds. This is not all. So many contingencies may arise and it will be the duty of a sound concern to arrange for each and every one of them. Profits anticipated may result in loss before the stock in hand is disposed of, either because prices have gone down or because the demand for the same has changed. Contracts for future delivery or future purchase may or may not result in profit. Sometimes, commodities may be transferred from one store to another at a price above cost. These and various other factors well-known to businessmen and accountants should be taken into account before the profits of a concern are calculated.

Thus we have seen that in a study of Business, Economics with its tools developed so far is of little or no use. In a study of technical problems, in many cases, the subject can be pursued satisfactorily in isolation and the results so obtained by isolated studies can then be applied to practice without any material loss of the usefulness of the results achieved. In fact, this is the method in scientific investigations, the results of which are achieved in the laboratory and subsequently applied to practice. But a study of economic problems is of entirely different nature. The problems of the economic structure are so interconnected and interdependent that the study of a particular aspect of it carried on in isolation is of little use. It may be said that different problems of economic structure may be studied differently and the results achieved by these different studies may be connected together for the building

up of a consistent whole; but the final result thus achieved may be entirely different from reality. For these different problems are not of the same nature as the different parts of a machine connected together. They are organic, so to say, one influencing the other in a manner not always detectable. To take one illustration, so many master minds have upto this time studied the problem of the trade cycle and so many different theories have been put forward. According to some it is purely monetary phenomenon, according to others it is the result of over-investment or under-consumption or psychological factors. There is no doubt that none of these explanations taken separately can explain the phenomenon of the trade cycle; each one of them is playing its part at different stages of the cycle in different proportion. This organic character is inexplicable by isolated studies. "Abstract economic analysis, itself, of course, presents no difficulty, as the abundant literature on the subject sufficiently testifies. What is lacking is any effective means of communication between abstract theory and concrete application."

In view of these difficulties the analytical economist wants more time for perfecting his tool. He admits, though reluctantly, that "the theory of Economics does not furnish a body of settled conclusions immediately applicable to policy," and that "the gap between the tool-makers and the tool-users is a distressingly wide one." But the economist is not yet in a position to answer to the queries of the practical man; he cannot give "bread," instead, he gives "stones." What is more tragic, even his tools are not yet prepared for the study of reality, and he has to "plunge into the tangled problems of the real world armed only with his naked hands."

Need for Business Education.

Businessmen are born, not made. Successful business requires certain qualities of the brain. But under present-day conditions, business education has indisputably become a dominant factor in advancing the economic efficiency of any country. For, although business requires natural qualities, acquired qualities are also essential for the proper development and utilisation of the former. For that purpose, business educa-

tion must proceed on most carefully planned lines and this responsibility should rest with the state, to be supplemented by the efforts of the rich business magnates. There can be no better form of national investment than to train up the youngmen of the country in business. In fact, the problem of personnel is one of the stumbling blocks in the way of the development of business of any country.

In this respect, we suffer for two reasons. In the first place, the nature of education imparted in our country is defective. For, problems affecting the factory organisation and management, such as, factory planning, production planning and progress, labour organisation and welfare, stores control, cost accounting and control, time and motion study, fatigue research, vocational tests, industrial psychology, wages and efficiency systems and budgetary control, etc., and business organisation, such as, market research, advertising, etc., have scarcely received any attention so far. Not only that; even the subjects taught are more or less the same as in Economics. We have already seen how the study of Economics is of little use in the field of business. Secondly, the output of commerce graduates is gradually increasing. In view of the inadequate development of business in our country, this increasing supply cannot be conveniently absorbed. Both these aspects need reforms. On the one hand, business education should be introduced in proper sense of the term; and on the other hand, suitable opportunities should be created for the absorption of competent commerce graduates.

Business education should not end in the educational institution, but should be supplemented by practical training simultaneously. What is needed is an idea of the actual operation, for, a study of business atmosphere is thousand times more important than the bookish knowledge and one hour spent in actual business is worth the whole day's study. This aspect of business education does not seem to have received much attention in our country upto this time.

PART I.

CHAPTER II.

FORMS OF ORGANISATION.

Single Owner.

The commonest type of businessman in this country as in any other country is the single owner, or sole trader, as he is often called. The organisation aspect of the sole trading concern presents very few things which may be of any particular interest. The sole trader carries on business on his own account. When the sole trading concern is being run on a small scale, there is no need for engaging an employee; every work is done by the owner with the help of the elderly members of his family. Sometimes one employee may be taken to render assistance in some work. But when the sole trading concern expands, the ownership and responsibility though shouldered by one, the functions may be distributed, sometimes among the different members of the family and sometimes among the hired employees. The sole trader may bring in his own capital or supplement it by deposits from friends and relatives or borrowings from the financial institutions; and it is he who alone is responsible for profit or loss in business. So far as he depends on borrowed money, his liability is unlimited and if his business creditors cannot be paid in full out of his business assets, the balance due to them will have to be paid out of his private savings or property, if any.

The sole trader is at a greater advantage in so far as he can take greater personal interest in business, which, in its turn, leads to efficiency and economy. Like partnership, but unlike joint stock company, the formation of a sole trading concern needs no legal formalities. At the same time, it has greater advantage over partnership in so far as the owner of the business is the master of all he surveys and this facilitates quick decision and prompt action which is not always possible or may be hampered owing to the existence of a number of

partners in a partnership. Death, insolvency and insanity will naturally lead to a dissolution of the partnership firm unless, of course, it is renewed. In the sole trading concern, the ownership is hereditary and death of the owner need not lead to dissolution of the concern. It has great advantage over a Corporation in business where local need is to be satisfied and where taste and fashion are paramount.

But the sole trading concern has its disadvantages as well. Difficulties of supervision on the part of a single individual in a big concern, though alleged as one of the drawbacks, cannot be regarded as such in these days of functional allocation to hired employees. Another drawback often pointed out is the limited supply of capital at his disposal and it is argued that in these days in most trades huge capital is needed which is beyond the capacity of most trading concerns. This sort of difficulty was seen in England in the second decade of the present century when as a result of bank amalgamations and development of branch banking the banking institutions lost the intimate touch with petty traders in the interior. In our country also with the gradual ousting of the moneylenders as a result of stringent legislations and of the indigenous bankers owing to the development of modern banking and also because of the cautious lending policy pursued by the banks including the Reserve Bank of India and the Imperial Bank of India, the sources on which the sole traders could draw have been limited. But this difficulty seems to be short-lived. With the gradual adjustment of the indigenous bankers to more scientific line of banking transactions and with the change in over-cautious attitude of banks, the temporary difficulties of the sole trader will be over. Another difficulty of a sole trader,—this argument does not apply to a sole trading concern on a large scale—it is alleged, lies in the purchase and sale of goods. The economies of bulk purchase and increased turn over, particularly when the sale is to be effected outside the locality or province in which the shop is situated, cannot be availed of by petty traders. But even in this respect the advanced commercial countries have found out solution in group-purchase and group-sale which may be adopted by the petty traders in this country. So far as purchases in foreign countries are concerned, we have got Indent Firms whose function

is to obtain orders from different concerns and place orders wholesale. In inland trade, however, the strict secrecy that the traders want to preserve has stood in the way of the adoption of group-purchase. But the most fundamental difficulty of a sole trader lies in the field of liability; for, as already noted, his liability is unlimited. But then he cannot get rid of it in view of the particular nature of the organisation of his business. Where everything depends on the ability and judgment of a single individual, there is no sense in making his liability limited without at the same time jeopardising the standard of business morality. In any case, in spite of these drawbacks and disadvantages, alleged and real, the sole trader is no rarity even in advanced commercial countries of the world.

Partnership

The law governing partnership in India defines it as "the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all." Three elements are quite distinct in a partnership. In the first place, there must be an agreement among the partners and their relationship must be the result of a contract. Thus the heirs of a deceased partner do not become partners by merely succeeding to the assets of business. If they want to be partners, they must enter into a voluntary contract with the surviving partners, provided the latter give their consent to take them in, and this voluntary contract must be a contract with regard to the business of the firm. Secondly, the object of the agreement must be the sharing of the profits of business. Thirdly, the business of the firm must be carried out by all or by one or more of the parties to the agreement working for all.

The definition of partnership in the English law is very similar to that given above. In English law, the partnership is defined as "the relation which subsists between persons carrying on a business in common with a view to profit." It must however, be noted that the English law of partnership does not recognise the firm as distinct from partners constituting it. The Indian law has not departed from the principle laid down by the English law in so far as it does not recognise the

partnership as a legal entity; but at the same time it must be admitted that the Indian law is a distinct improvement over the English law in so far as it emphasizes, apart from the abstract relationship of different partners *inter se*, the concrete aspect of the firm. Persons who have entered into partnership agreement with one another are individually called "Partners," and collectively a "Firm" and the name under which the business of partnership is carried on is called the "Firm Name."

Three kinds of partners may be distinguished. In the first place, there are active partners who bring in capital and take active interest in the business of the firm. Secondly, there are sleeping or dormant partners who bring in some capital but do not take any active interest in the conduct of business. And thirdly, there are nominal partners who neither contribute any capital nor take any active part but simply lend the use of their names and credit to the firm.

Partners, when they carry on business on behalf of the firm, are agents as well as principals—principals in their mutual relation but agents when working on behalf of the firm and in their relation to third parties. All partners need not necessarily be engaged in active transaction of business. It may be in the hands of one or more than one working for all. So long as the partners are working as agents of the firm, any liability incurred by them is the liability of the firm. Any liability incurred by a partner acting on his own behalf and not on behalf of the firm will in no way affect the firm.

The essential feature of partnership is mutual confidence and mutual trust. The selection of partners should therefore be made with utmost caution, and should be restricted to a narrow circle in which full confidence may be placed and about whose honesty and integrity no partner has the slightest reason for doubt. For, the law is clear that every partner is responsible to his last pie for the debts of partnership incurred in the course of its business, no matter however small the share of an individual partner may be in the firm. This being the case, a partner with small share and poor resources may, by his negligence or dishonesty, place the whole firm in trouble and bring ruin on other partners. This in itself is a sufficient reason for the careful selection of partners.

As regards the number of partners in a partnership firm, the law in this country places limit on the number of persons who can enter into partnership agreement. If the business is of a general type, the number of partners should not exceed twenty; but in case of banking business, the maximum number of partners in a firm is ten. Partnership firms carrying on general business may also have banking as side business and *vice versa*. There are very few partnership firms carrying on banking on European lines along with other business. The most noted of such firms is Messrs. Thacker Spink & Co., having stationery, books and banking departments. Another partnership firm carrying on banking side by side with other types of business, such as, insurance, gunny, coal, etc., is Messrs. Gillanders Arbuthnot & Co.

A partnership can be entered into by an oral agreement but such a course is not desirable, for, in time, it becomes a fruitful cause of misunderstanding and litigation, leading to a collapse of the firm. Hence it is desirable on the part of partners to enter into a written agreement, known as Deed of Partnership. The Deed contains all details as to the amount of capital contributed by each partner, the proportion in which profits are to be shared among them, the limit of monthly drawing of each partner, the rate of interest, if any, to be charged on drawings and paid on capital, the basis for calculation of goodwill in case of retirement or death of a partner, and so many other things so that there may not be any scope for dispute, or it may be avoided as far as possible. The Deed also contains an Arbitration Clause, according to which all partners agree to refer any dispute to an arbitrator and abide by his decisions.

The rights and duties of the partners have been distinctly laid down in the Indian Partnership Act, 1932. Partners are bound to carry on the business of the firm to the greatest common advantage, to be just and faithful to each other and to render true accounts and full information of all things affecting the firm to any partner or his legal representative. Since the business is to be carried on by all partners or by some acting for all, it follows that they have pledged to do so in such a way as to obtain the greatest common advantage. In conducting the business of the firm, no partner will be allowed to

make personal profit out of it. But this prohibition does in no respect stand in the way of a partner's deriving personal profit in respect of matters not lying within the scope of, and not involving competition with, the business of the firm, even if he does so by using information derived in the business itself. Every partner shall indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm.

Turning, next, to rights enjoyed by partners, every partner has a right to take part in the conduct of business, unless, of course, by an agreement, the conducting of business is entrusted to one or a few of them, to the exclusion of other or others, in which case the latter cannot participate in business. But this restraint is voluntary. Every partner is bound to attend diligently to his duties in the conduct of the business. Where a partner throws the whole conduct of the business on another partner, the latter is entitled to receive remuneration. Apart from such special circumstances, no partner is entitled to any remuneration, other than the due share in profit earned, for taking an active part in business. Any difference arising as to the ordinary matters connected with the business may be decided by a majority of the partners; every partner shall have the right to express his opinion before the matter is decided, but no change may be made in the nature of the business without the consent of all the partners. Every partner has a right to have access to and to inspect and copy any of the books of the firm.

The mutual rights and liabilities of the partners of a firm may be determined by contract between the partners, express or implied, such contract being varied only by consent of all the partners. Some of the mutual rights and liabilities are indicated below:

(a) A partner is not entitled to receive remuneration for taking part in the conduct of the business;

(b) All partners are entitled to share equally in the profits earned and are liable to contribute equally to the losses suffered by the firm;

(c) Where a partner is entitled to interest on the capital subscribed by him, such interest shall be payable only out of profits. A partner making, for the purpose of the business, any payment or advancing beyond the amount of capital he has

agreed to subscribe is entitled to interest thereon at the rate of six per cent per annum.

(d) The firm shall indemnify a partner in respect of payments made and liabilities incurred by him;

(i) in the ordinary and proper conduct of business; and

(ii) in doing such act, in an emergency, for the purpose of protecting the firm from loss, as would be done by a person of ordinary prudence, in his own case, under similar circumstances;

(e) a partner is bound to indemnify the firm for any loss caused to it by his wilful neglect in the conduct of the business of the firm.

So far we have considered the mutual relations of the partners. Now we shall turn our attention to the relation of partners to third parties. We have already seen that while conducting the business of the firm, the partner is an agent of the firm. Subject to the provisions of Section 22 of the Indian Partnership Act of 1932, the act of a partner which is done to carry on, in the usual way, the business of the partnership firm, will be binding on the firm by "implied" authority, which flows from the legal relationship of the partners. The "express" authority is, however, conferred upon him expressly by the actual contract between the partners. Whether the authority is expressed or implied, an act done by a partner in the usual course of business binds his co-partners and makes them liable to third parties dealing with him as agent of the firm.

In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to:

(a) submit a dispute relating to the business of the firm to arbitration,

(b) open a banking account on behalf of the firm in his own name,

(c) compromise or relinquish any claim or portion of a claim by the firm,

(d) withdraw a suit or proceeding filed on behalf of the firm,

(e) admit any liability in a suit or proceeding against the firm,

(f) acquire immovable property on behalf of the firm.

- (g) transfer immovable property belonging to the firm, or
- (h) enter into partnership on behalf of the firm.

Section 22 of the Indian Partnership Act, 1932, declares that an act done on behalf of a firm does not bind it unless it is done in the name of the firm or in some way indicating that it is done with the intention of binding the firm. Every partner is liable, jointly and severally, for all acts of the firm done while he is a partner.

A partner has authority, in an emergency, to do all such acts for the purpose of protecting the firm from loss as would be done by a person of ordinary prudence, in his own case, acting under similar circumstances and such acts bind the firm.

The next question is, who can be a partner? Naturally, the persons who had formed the partnership firm are partners. Where a person holds himself out as a partner, or allows others to do it, he is estopped from denying the character he has assumed and upon the faith of which his creditors may be presumed to have acted. A man so doing may be rightly held liable as a partner by estoppel, even though he has not contributed either labour or capital and has no interest in the profits of the business or is indemnified against all possibility of loss. A former partner does not become a partner by estoppel merely because the firm has continued to use its old name, of which his own name forms a component part. The rule of estoppel is binding on a former partner who has retired without giving proper notice of his retirement. A new partner would not however be liable to a creditor of a firm who did not know him to be a partner in the firm, although in fact he was a partner of the firm, because the creditor could not be supposed to have dealt with the firm on the knowledge of this fact.

A partner may retire (a) with the consent of all the other partners, (b) in accordance with an express agreement by partners, or (c) where the partnership is at will, by giving notice in writing to all other partners of his intention to retire. A retiring partner may be discharged from liability to a third party for acts of the firm done before his retirement by an agreement made by him with such third party and the partners of the reconstituted firm. Notwithstanding the retirement of a partner, he continues to be liable to third parties until he gives public notice of his retirement.

The case of a deceased partner stands on a footing different from that of a partner retiring during his lifetime. On the death of a partner, neither his legal representatives nor his property can be held liable for transactions after his death, though the business is continued by the surviving partners under the old name, or under a name of which the name of the deceased partner forms a part and though the old customers and creditors have no notice of his death.

As regards the introduction of a new partner, no person can be introduced as a partner into a firm without the consent of all the existing partners. A person who is introduced as a partner into a firm does not thereby become liable for any act of the firm done before he became a partner. We have already seen that the underlying feature of a partnership is mutual trust and mutual confidence. But this may be hampered by the introduction of a stranger in the partnership firm. But where all partners agree to such an introduction, this problem does not arise at all and the smooth working of the firm remains ensured.

The Indian Partnership Act of 1932 has introduced a new feature in partnership business by introducing registration of a firm, which may or may not be availed of by a particular concern. Registration is not compulsory, nor does it impose any penalty for non-registration. But then if there is no inducement to register, the provision would remain a dead letter. So the law has imposed certain disabilities on unregistered firms and partners, thereby bringing an indirect sort of pressure to bear upon them to register. Thus although we cannot say that the chapter on registration of firms is really an integral part of partnership law, yet its importance in the field of business cannot be entirely neglected.

The idea of registering firms is not a new one and proposal for registration, sometimes for compulsory registration, have been put forward, but in view of the inherent difficulties in the way of such a legislation in India where many firms are governed under the Hindu Law, the opinion of the mercantile community of the country differed and the government also became hesitant in taking any such step. This conflict with the existing law was not the only difficulty. There was a greater difficulty still. Under the Hindu Law prevalent in greater

part of the country, every new birth of a male child adds to the number of partners in the Hindu joint family business, just as every death of a male member subtracts from their number. If the registration of a partnership firm is made compulsory, it would be very much inconvenient in so far as every birth or death and every partition of family would necessitate a change in the register. Many partnership firms are temporary in character, sometimes for the transaction of a particular business; and as soon as the business is over, the partnership is dissolved. If registration is made compulsory, this sort of enterprise would surely be hampered and be forced to evade the provisions of the law; while at the same time the benefit derived from the public may be, and will be, negligible. The same would also be true with regard to firms carrying on petty business. In these cases the transactions are limited within a narrow circle and enforcement of claims in the court of law is a rare phenomenon, whereas the procedure of registration would always exercise a damping effect on the formation of partnership. Under these circumstances, it is not possible to understand the plea of the British mercantile community in this country in favour of compulsory registration, as prevalent in England. They went further and even suggested that the provision for compulsory registration should apply even to the Hindu joint family business.

The framers of the Indian Partnership Act, however,—it must be admitted,—took a reasonable view of the situation and tried to obtain the advantages of registration without at the same time giving up the advantages of the existing system, nor did they want to interfere with the working of the Hindu joint family business under the Hindu Law. They therefore wisely confined their attention to ordinary partnership firms which are contractual in their origin. It was also considered that by making registration optional and offering substantial inducements to register, all the benefits of registration would be retained without at the same time introducing the distasteful feature of compulsion. Under the existing legislation, any firm, which is not registered will not be able to enforce its claims against the third party in the civil courts and any partner who is not registered will be unable to enforce his claims against the third party or against his fellow partners. On

the other hand, third parties are free to enforce any claims they may have against unregistered firms or partners in such firms.

The only particulars to be furnished to the Registrar for registering a firm are the name of the firm, the place or places of business, the date on which each partner joined the firm, the names and permanent addresses of the partners and the duration of the firm. It should be noted that unlike in the case of a joint stock company, registration in the case of partnership does not involve the disclosure of any internal affairs of the firm. This is due to the fact that any information regarding the internal affairs of the firm is useless to the public in so far as a partnership firm cannot issue shares to the public. The Registrar being a recording officer will simply record the statement made by the firm without going into its accuracy. Changes in the firm name, or its principal place of business, may be reported to the Registrar in order to enable him to bring the register up-to-date. The reporting, unlike in a joint-stock concern, is not obligatory; but it needs to be done in order to become consistent with all the legal formalities.

On the effects of non-registration of a partnership firm, the Act is quite clear. The position is given in the following sub-sections of Section 69 of the Act. The sub-sections are as follows:—

(1) No suit to enforce a right arising from a contract or conferred by this Act shall be instituted in any court by or on behalf of any person suing as a partner in a firm against the firm or any person alleged to be or to have been a partner in the firm unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner in the firm.

(2) No suit to enforce a right arising from a contract shall be instituted in any court by or on behalf of a firm against any third party unless the firm is registered and the persons suing are or have been shown in the Register of Firms as partners in the firm.

(3) The provisions of sub-sections (1) and (2) shall apply also to a claim of set-off or other proceeding to enforce a right arising from a contract, but shall not affect

(a) the enforcement of any right to sue for the dissolution of a firm or for accounts of a dissolved firm, or

any right or power to realise the property of a dissolved firm, or

(b) the powers of an official assignee, receiver or court under the Presidency Towns Insolvency Act, 1909, or the Provincial Insolvency Act, 1920, to realise the property of an insolvent partner.

(4) This section shall not apply

(a) to firms or to partners in firms which have no place of business in British India or whose places of business in British India are situated in areas to which, by notification under Section 55, this chapter does not apply or

(b) to any suits or claim of set-off not exceeding one hundred rupees in value which, in the Presidency-towns is not of a kind specified in Section 19 of the Presidency Small Causes Courts Act, 1882, or outside the Presidency-towns, is not of a kind specified in the second schedule to the Provincial Small Cause Courts Act, 1887, or to any proceeding in execution or other proceeding incidental to or arising from any such suit or claim.

In England another type of partnership firm has come into existence under the Limited Partnership Act, 1907. This is known as Limited Partnership. In a limited partnership firm, a general partner enjoys similar rights and is subject to similar liabilities as in ordinary partnership. On the contrary, the rights and liabilities of a limited partner are limited. The limited partner makes a fixed contribution to the partnership business which he cannot withdraw during his limited partnership. He takes no part in the management of the firm. He may inspect the books of the firm and can tender advice, but cannot in any way bind the firm. Death, bankruptcy or lunacy of a limited partner will not lead to a dissolution of the firm, as it would happen in ordinary partnership. A limited partner in general, cannot object to the introduction of a new partner, nor can he dissolve the firm by giving notice; but he may assign his share to somebody else who becomes a limited partner in his place. Be it noted, however, that undertakings of this type are not numerous, greater attraction being offered by the facilities that now exist for the formation of private companies with limited liability under the Companies Act.

Hindu Joint-family Firm.

A joint family firm is the creation of Hindu Law; the rights and liabilities of the co-parceners owning a joint family business are determined by the Hindu Law and not by any Act of the Indian Legislature. In the case of such a family, every male member born in the family acquires by birth a share in the business. As regards the liability of the members of a family business, the *karta* or manager is personally liable to an unlimited extent, though other members of the family are liable only to the limited extent, i.e., to the extent of their interest in the firm, unless they are parties to any transaction or contract entered into by the manager. It is interesting that from the standpoint of liability, the joint family firm resembles the limited partnership concerns to be found in England. For, the liability of the *karta*, like that of a general partner, is unlimited, whereas that of other partners, like that of limited partners, is limited. They are only liable to the extent of the joint-family property; private property, if any, will remain untouched. The point of similarity with limited partnership does not end here. As regards management also, there is some similarity. The manager of a joint-family business has larger rights in the management than any other partner. Thus the manager has an implied authority to pledge the property of the family for the benefit of the family business. He can enter into contracts, give receipts and compromise and discharge claims arising out of business. But other partners, like limited partners, cannot interfere in any way in these matters.

If the manager of a joint family business, acting on behalf of the family, enters into a partnership with a stranger, every partner of the family business does not become a partner of the new concern thus brought into existence and the relation of the family business with the new concern terminates on the death of the manager, who is, so to say, a link between the two. Just as other partners have nothing to do with the new concern during the life-time of the manager, so also after his death they are in no better position than sub-partners vis-a-vis that concern.

Another interesting point to note in connection with joint family firm is that it is not dissolved by the death of a co-parcener, nor is a co-parcener entitled, on severing his con-

nection with the family firm, to ask for accounts of past profits and losses.

Although in some respects the joint family firm resembles other types of concern known in the Western world, it must be admitted that it is a type by itself and a product of the Indian soil. Unlike in an ordinary partnership which is contractual, its Indian prototype arises from status in the family, and is formed by the male issues. Unlike in a joint stock company where interest is acquired by going in for shares of the company and by having their names entered in the register of members, the interest in joint family business is acquired by birth. But the co-parceners in a joint family business, like the shareholders of a joint stock company, are more or less sleeping partners, everything being done by the manager in the former and the Board of Directors or Managing Director in the latter, nor is their existence affected by the lunacy, bankruptcy and death of a co-parcener or a shareholder. In this respect the difference from partnership is remarkable, for, in a partnership, unless otherwise arranged, each and every partner can, as a matter of right, participate in the business of the concern, and the partnership is dissolved by the death, bankruptcy or lunacy of any one partner, though, of course, it may be revived by the existing partners if they so desire.

CHAPTER III

FORMS OF ORGANISATION (Contd.)

Advent of Joint-Stockism.

With the growing complexity of business which needed sound businessmen for its successful continuation and with the increase in risk, a new type of business organisation has come into existence, *viz.*, the joint stock company. Its advent has made possible gigantic enterprises, under the guidance of business experts, pooling its financial resources from the savings of all classes of men, both rich and poor, and at the same time limiting the liability of the proprietors, thereby removing the terror of investment. In fact, the movement in favour of limited liability in some western countries was the outcome of the failure of some concerns as a result of which many proprietors had burnt their fingers and some reduced to the state of abject poverty. The outcome was the legal recognition of the principle of limited liability. Thus some people have gone so far as to declare the Joint Stock Company as the extension of partnership firm, the disadvantages of the latter arising out of unlimited liability being removed by the substitution of limited liability.

There was another reason for the advent of the new type of organisation. Since the rise of industrialism every big venture requires a huge capital which is outside the availability of a partnership, what to speak of a sole trader. Besides, so far as the small saver was concerned, his small saving—though individually insignificant, but collectively a fair proportion of national saving—could not be utilised. For, in a partnership, the finance was received from within a narrow circle, and no public call was issued. Both these problems were solved by the new type of business concern. On the one hand, the joint stock concern can raise enormous sums by floating shares and debentures, and on the other hand, it has given scope to all types of investors by making the denomination of each share very small, so that even the smallest saver can have his money

invested. In fact, even the manual labourers in a concern are sometimes found to be the shareholders of the same or other concerns, thereby having not only a share in the annual profits of the concern but also having a voice,—as much as is allowed to the shareholders—in the management of the concern through their control over directors.

What is a Company?

Ordinarily speaking, a company, like any other association, is a body of persons formed for the attainment of some common purpose. But this general definition is not enough to distinguish a company from any other association. In strict sense, however, in a company, unlike in a partnership, the number of members is more numerous, and sometimes, as in the case of a public Joint Stock Company, there being no upper limit to their number, the interest of the members in the business being transferable even without the knowledge and consent of other members. It is these two features, *viz.*, unlimited or more numerous number of members and transferability of share, that distinguish a company from any other type of business concern known so far.

The points of distinction however do not end here. To note a few more points of contrast,—in the first place, a company comes into existence by the special process of registration under the Indian Companies Act along with subsequent amendments, by special statute or by Royal Charter: no such legal formality is called for in any other type of concern, the registration in case of partnership, though provided for, being optional. It follows from this, secondly, that while in a sole trading concern, the sole trader is his own master and in partnership the personal relation of the partners *inter se* is all important, in a company the personality of the individuals who join together to form the company is merged in the legal entity thus created. A company is a legal, artificial “person” having its own name and seal, with rights and liabilities entirely distinct from those of the members who compose it. In a partnership, any partner may bind the firm and any partner may be called upon to pay the debts of the firm. But the rights and obligations of a company are distinct from the rights and obligations of its individual members. Only the officers of the company acting in its

name can exercise the company's rights; the shareholders having nothing to do in this respect. Thirdly, when a company is limited by shares or by guarantee, no member can be made to contribute to the company's assets anything beyond the sum, if any, still unpaid on the shares he has taken or on the guarantee he has given. But, we have already seen, the liability of a partner is unlimited; even in case of limited partnership, the liability of a general partner is unlimited. Fourthly, if a member of a company sells his holding, neither his withdrawal nor the entry of his successor, makes any difference to the existence of the company. Even the death, lunacy or bankruptcy of a member does not affect its continuity; not so in case of a partnership. Fifthly, as already seen, every partner has the right, unless he otherwise agrees to cede it in favour of one or more partners and unless he is a limited partner or a co-parcener in a joint family business, to participate actively in the management of the firm's affairs; but the rights of shareholders are very much restricted and can only be exercised in some prescribed way, e.g., by formal resolution in general meeting, or by application to the court in some special circumstances. Sixthly, the constitution of a firm may be changed by agreement among the partners; but any alteration of a company's memorandum, changing thereby its object clause, or reducing its capital or modifying the rights attaching to its shares cannot be made without the consent of the court. Finally, a company, by keeping its books open for inspection and by filing returns with the Registrar, is required to make public certain information which in a partnership firm, even though registered, may not be known to outsiders. The reason for this is obvious. In the case of a joint stock company, the interest of the public is involved in so far as they are the investors in the concern. Any false information may involve the members of the public and put them in bad investment. Not so in case of partnership, even when it is registered. It is on all these grounds that a company differs from a partnership or any other type of business concern.

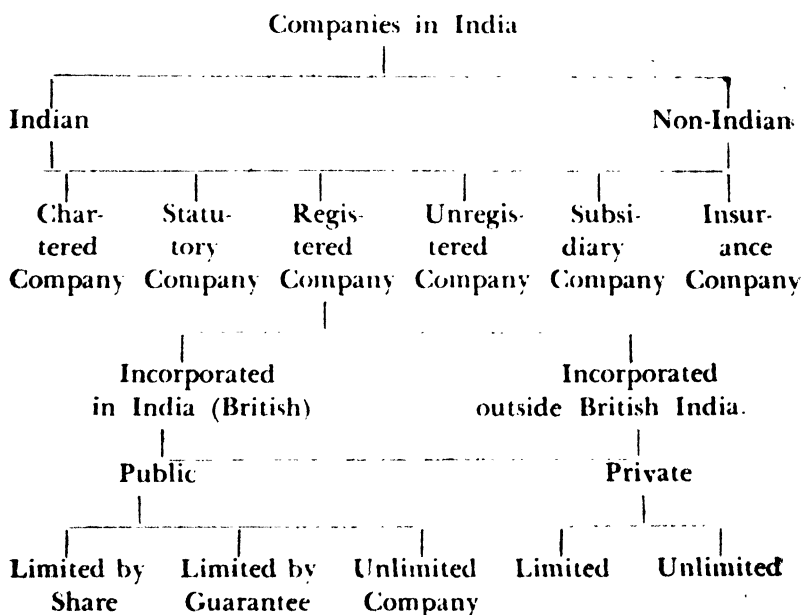
History of Company Law in India.

The first Company Law in India, the Joint Stock Companies' Act, was passed as early as 1850, which was followed by

two Acts of 1857 and 1860, all the previous Acts being repealed by the Companies' Act of 1860. This Act, in its turn, was repealed in 1882 and it remained in force till 1913 when an extensive amendment to the Companies' Act was passed. The Act of 1913 was based on the English Companies' Act of 1908, with certain additional provisions to meet the peculiar conditions prevailing in India. It not only extensively amended the previous legislation relating to trading companies and other associations in British India but was also a consolidating Act. In time, however, the deficiencies of the Act of 1913 came to light; for, it did not provide for certain peculiarities of Indian commerce, such as, the managing agency system, and in certain other respects it was found to be highly unsatisfactory in its operation. The Indian Companies (Amendment) Act of 1936 has sought to remove these deficiencies. The Act has since been further amended almost every year in order to make it more suited to existing conditions in the field of business.

Types of Companies in India.

The types of companies can be best illustrated with the help of the following chart:—



We shall consider the above classification in brief, devoting much of our attention to the Public Company, limited by share, which is by far the most important. To take up the Chartered Company first, a company incorporated by a Royal Charter has an unrestricted corporate capacity as an ordinary person. At the time of granting the charter, its power may, however, be limited in a direction, such limitation being only an essential part of the so-called bargain between the crown and the company. Notwithstanding this limitation, however, the company has been granted plenary capacity in the common law in England and all that the crown can do is to annul the charter, as was done in the case of the East India Company. It is in this respect that a chartered company organisation differs from any other type of business organisation; for whereas in case of any other company the object is limited and can in no case be transgressed, the chartered company enjoys plenary capacity in the common law.

A statutory company is a company incorporated by a special Act of the Legislature. Companies in relation to railways, docks and gas, electric and tramway undertakings are usually incorporated by such Acts. The only point of distinction between the statutory company and a registered company lies in powers granted. So far as the statutory companies are concerned, they are invested mostly with compulsory powers. But in a company formed otherwise, the directors have always got discretion with regard to the exercise of powers conferred on them by the Memorandum of Association and Articles of Association of the Company. Leaving aside this fundamental point of distinction, a statutory company is very similar to the registered company's constitution.

An unregistered company is nothing but a big partnership, constituted by contract, some of its features being akin to those of a registered company. These features are transferability of shares, continuity of the concern, notwithstanding the death or bankruptcy of one or more members and the vesting of the management in a selected body of directors, to the exclusion of members. But as regards the liability of the members, this type of business organisation is akin to partnership.

Another variety of companies to be found in India are insurance companies. To place them under a separate heading

may at first sight seem unnecessary, but this has been done because they are governed by an Act of their own. The business of insurance is essentially contractual but it raises several problems to itself, this being the reason why the Contract Law alone was insufficient and the need for a special Insurance Act was felt. Before the passing of the Indian Life Insurance Companies Act of 1912, the Companies were governed either by the Act X of 1866, or the Assignment of Fire and Marine Policies, or by the Indian Companies Act of 1882. The expansion of Indian insurance business during the days of the swadeshi movement necessitated the passing of a separate insurance law with regard to the life insurance business, in which line the Indian concerns have specially proceeded, with a view to check the mushroom growth of bogus companies. The Indian law is based more or less on the principle laid down by the British law in this respect, *viz.*, minimum amount of interference with the working of the company with maximum amount of publicity so as to enable the public to decide for themselves, while at the same time insisting on a certain amount of deposit being paid in, not with the object so much of protecting the policyholders as of preventing the formation of mushroom companies. With this principle underlying, the Act of 1912 was passed. This Act was seriously defective in so far as it did not govern insurance business other than life and thus gave a freehand to the foreign companies which have a practical monopoly of this type of insurance business. The modified Act of 1938 applies to all types of insurance business transacted by companies incorporated in British India, United Kingdom or elsewhere. To prevent the growth of mushroom companies, the Act provides for registration of all companies and a substantial initial deposit of Rs. 50,000/- in securities to be raised to a total of Rs. 2,00,000/- within a stated period. The Act provides for refusal to register unless a sum of at least Rs. 50,000/- is collected for working capital, over and above the sum necessary to meet compulsory deposit. The filing of statements and accounts with the Superintendent of Insurance has been made compulsory even with regard to the British and foreign companies, on penalty of prosecution and even winding up in case of non-compliance. This stringent but necessary restriction was modified in 1941 with a view to adjust the business with the changed

situation, and the Insurance Amendment Act of 1941 permitted the payment of reduced instalments of deposits during the continuation of war and one year afterwards by the companies doing life insurance business only, who commenced to issue life policies during the ten years prior to the outbreak of war on 3rd September, 1939. This relief was granted, subject to conditions, to such small insurance companies as were experiencing a fall in new business and of lapse of existing policies due to war.

Next we turn to another type of companies which in this country have been regarded with the greatest possible disfavour. They do not differ from other companies in the matter of constitution and function. But the only point of difference, and a vital one, lies in their non-Indian origin. They are to be found in almost all lines of business, some of them being their virtual monopoly, *e.g.*, jute industry, coal mines and tea gardens. In the wider field of commerce also, *e.g.*, foreign exchange, insurance other than life, etc., they have a preponderating influence and control. The unsympathetic attitude of some of these foreign exchange banks was revealed in the evidences tendered before the *Indian Central Banking Enquiry Committee*. The high freight charged by foreign shipping along with other troubles placed in the way of Indian commerce is equally well-known. In the field of insurance business other than life, also, the control of India's foreign trade by foreigners has stood in the way of development of Indian companies in this particular line. Thus if a firm of managing agents represents a particular company, all the insurance business of that particular company goes to the insurance companies represented by that firm. Even when the managing agents happen to be an Indian concern, a major portion of business goes to non-Indian companies because the managing agents happen to represent British and other non-Indian insurance companies. Sometimes, the importers in other countries stipulate in their letters of credit that insurance should be effected with such and such concern, with the result that the exchange banks working in India accept the documents only if the goods concerned are covered by that insurance company, which invariably is non-Indian.

The Indian opinion has all along been in favour of including certain provisions in the law which may give some

tangible help to Indian concerns. But neither the Insurance Act of 1938 nor the Banking Bill has done anything in this respect. The Indian Companies Act, however, lays down certain requirements of a minor character to be observed by companies which are incorporated outside British India and which also have offices and places of business in this country. On observance of these requirements, such companies come within the purview of the Indian Companies Act and therefore all provisions which would apply to companies established and incorporated in this country under the Act would equally apply to such foreign companies. The Indian Companies (Amendment) Act of 1936 adds a few more provisions which are in the nature of restrictions on their powers of management.

The Indian Companies (Amendment) Act of 1936 brings under the purview of the Act another variety of companies, called subsidiary companies, of which we shall note details in a subsequent chapter.

Registered Companies.

To consider the registered companies, they may be of two types, private and public. Before we consider these two types, we should note the cases where the law requires expressly the registration of a company. Where an association is formed for the purpose of carrying on banking business with more than ten individuals, it must of necessity be registered under the Companies Act. Registration is also compulsory in case of concerns carrying on general business with more than twenty individuals. If not registered, these associations will be regarded as "illegal" although none of the objects for which they may have been formed are illegal. Registration of a banking concern with ten or less members and that of a general concern with twenty or less members are not necessary, although there is no bar to their being registered and acquiring a corporate status with all the powers and privileges conferred upon registered companies by the Act; but in that case there is a limit for the minimum number of members, seven in case of a public and two in case of a private company. The effect of non-registration will, however, be that the liability of members would be unlimited, although they will in no sense be regarded as

“illegal” associations, but can carry on business as partnerships or unincorporated companies.

Private Company.

A private company is a company which by its articles,

(1) restricts the right to transfer shares, where it has got share capital,

(2) limits the maximum number of members to 50, excluding persons in the employ of the company, with at least a minimum number of two members, and

(3) prohibits any invitation to the public to subscribe to its shares and debentures,

In comparison to English law, the Indian law is very narrow. In English law, a private company comprises of persons who have taken up shares when they were in the service of the company but have subsequently ceased to be in its employ. In Indian law however any such person who having purchased a share in a private company has ceased to be in its employ is excluded from the membership of a private company.

The private company arrangement is full of promise; for, it brings within the reach of partnership the blessings of limited liability and at the same time it affords scope for the expansion of the number of members to 50 and for raising a fairly large capital. This form of incorporation has proved so popular in England that the limited partnership concerns have not made much headway inspite of the legal privileges granted. The Indian Companies Act of 1913 has fully adopted the recognition and an increasing number of companies are being incorporated under this arrangement. If at any stage, it is thought desirable, to convert the private company into a public one, this can be done under Section 154 of the Indian Companies Act of 1913.

In India, however, private company arrangement has not proved so very popular as in England. This is clear from the number of private limited companies carrying on banking and allied business in India. Thus in Bombay in 1928-29 there were 13 private concerns registered as private banks. There were several other private financial concerns in that province doing banking business on a large scale; but they were not registered. There were several other concerns registered as

private banks for considerations other than that of transacting banking business. For instance, among the specified objects for which some of the companies have been started are the following: "Carrying on business as capitalists, financiers, concessionaires or merchants," "forming, promoting, subsidising and assisting companies, syndicates and partnerships of all kinds," "carrying on and transacting every kind of guarantee and indemnity business," etc. Among the foreign exchange banks in Bengal two appear to have been private limited companies. One of them, Messrs. Thos. Cook & Sons, incorporated in England, carries on banking business along with other business. The other, Messrs. Grindlay & Co., also incorporated in England, has placed the banking department and the passage and shipping department under one and the same management. The firm was originally a partnership, but was converted into a private limited company in 1924 at the time of its affiliation with the National Provincial Bank. The *Bengal Provincial Banking Enquiry Committee* gives the following list of private limited banks and allied institutions at work in Bengal during the year 1928-29:

<i>Banks and allied Institutions as private limited Companies.</i>	<i>Objects.</i>
1. Rajnagar Loan & Trading Co., Ltd. ...	Banking and moneylending.
2. The Jagadamba Loan Co., Ltd. ...	Moneylending.
3. The Pioneer Agency Ltd.	To carry on the business of banking and manufacture of oil, rice, silk and other fabrics.
4. Rosheya Trading and Banking Co., Ltd. ...	To give loans, to take various sorts of deposits and to cultivate paddy, jute, fruits, etc.
5. The Banking Corporation Ltd. ...	To carry on the business as traders, bankers, managers, agents, managing agents, etc.

<i>Banks and allied Institutions as private limited Companies.</i>	<i>Objects.</i>
6. Trading Syndicate Ltd. ...	To carry on the business of banking and trading in general, such as, dealing in paddy, rice, wheat, etc.
7. The Murshidabad Agency Ltd. ...	Banking.
8. The Lakshmi Loan Corporation Ltd. ...	Banking and money lending.
9. Trash Bank Ltd. ...	Banking.
10. Kumar's Credit Corporation Ltd. ...	Banking.
11. Adamdighi Kundu Bhra-tri Sangha Ltd. ...	To lend and receive interest on mortgage of moveable and immovable properties.
12. Calcutta Bank Ltd. ...	Banking.
13. Mahalaxmi Industrial & Trading Bank Ltd. ...	Banking.
14. Dacca Oriental Loan and Trading Co. Ltd. ...	Money lending and Banking.
15. Nehalia Loan Office Ltd. ...	Money lending.
16. Prabartak Bank Ltd. ...	Banking.

Under the Indian Companies Act of 1913, although legal recognition was accorded to private Companies by granting the privilege of limited liability to registered concerns, no special privilege, over and above those enjoyed by public companies, was granted to them. The Act of 1936 has granted certain special privileges, which are as follows:

(1) In a private company, the minimum number of members need not be seven; two members are enough.

(2) It is not necessary for a private company which are not the subsidiary companies of public companies to have any directors; but in case of public companies and also subsidiary companies of public companies, there must at least be three

directors. In a private company, there may be no director at all.

(3) Section 83B and 84, making provisions and imposing restrictions regarding appointment and advertisement of directors do not apply to private companies.

(4) In the case of a private company which is not a subsidiary of a public company, Section 91B which prohibits voting by interested director and which lays down that the presence of such director shall not count for the purpose of forming a quorum at the time of such voting and that if he votes, his vote shall not be counted, does not apply.

(5) If there be a director, his consent in writing to act as such and his contract to take up qualification shares need not be filed with the Registrar; nor is it necessary for him to sign the memorandum for any qualification shares.

(6) Section 91D which makes provisions regarding contracts made by agents or managers of a company on behalf of the company in which the company is an undisclosed principal does not apply to the case of a private company which is not a subsidiary of a public company.

(7) The provisions of Section 103 regarding postponing the commencement of business or the exercise of borrowing powers until the requirements of the Section are fulfilled do not apply to a private company. A private company can commence business immediately on registration. The provisions regarding minimum subscriptions and allotment do not refer to a private company.

(8) Out of the regulations of Table A which are made compulsorily applicable to public companies under the amended Section 17 of the Act, regulations 78, 79, 80, 81 and 82 regarding the rotation of directors shall not be deemed to be included in the articles of a private company unless it is a subsidiary company of a public company.

(9) It is not necessary for a private company to file with the Registrar a statement in lieu of prospectus.

(10) Section 77 which provides for the holding of the statutory meeting, the forwarding of a copy of the statutory report to every member of the company, and the delivery of a copy

of the statutory report to the Registrar for registration and other provisions of the Section do not apply to a private company.

(11) It is not necessary for a private company to send any copy of its balance sheet and profit and loss account or the income and expenditure account with a copy of the auditor's report to its members. But if a member of a private company wants to have from his company copies of the balance sheet and profit and loss account by paying for them, the company must furnish the copies.

(12) Section 134 which requires three copies of the balance sheet to be forwarded to the Registrar is not applicable to a private company.

(13) Under Section 144, in the case of a private company, not being the subsidiary of a public company, a person who does not hold certificate from the Central Government entitling him to act as an auditor of companies, may be appointed as an auditor of such a private company. A person in the employment of a director or officer of the company may be an auditor of such a private company not being the subsidiary of a public company.

(14) Section 146 which gives holders of preference shares and debentures of a company the same right to receive and inspect the balance sheets and profit and loss accounts of the company and the auditor's reports and other reports, as is possessed by the ordinary shareholders, does not apply to a private company so that a private company is not bound to allow these rights to preference shareholders and debenture holders.

The above exemptions and privileges remain valid so long as the company continues to observe the limitations and restrictions imposed upon it by the Act. But here arises a question of interest. If the company does not observe the limitations, would it cease to be a private company? The opinion of legal experts and some judicial decisions were in the negative. But in that case the limitations imposed on a private company become nothing better than dead letters. So the English Act of 1929 provides that in the case of default in the observance of the limitations or any other provision of the Act, the company

would cease to be a private company, unless, of course, it is relieved from these consequences by the court on an application made by the company or any other person interested in it, showing, to the satisfaction of the court, that the default was accidental or due to inadvertence or some other just cause. In India, too, the amendment Act of 1936 has introduced a similar provision.

(2) *Public Company.*

A public joint stock company is an association of a number of persons united for some specific business carried on under a certificate of incorporation granted by the Registrar of Joint Stock Companies and thereby formed into a body corporate, having a legal entity with its own name and seal, capable of holding property and contracting debts in its own name and having a separate existence from persons composing it. Public companies may be of three types,—those limited by share, those limited by guarantee and unlimited companies. Of these, the first type is by far the most numerous at the present time. In companies limited by guarantee, each member undertakes to be liable to pay the debts of the company upto a certain amount, but the capital of the company is not divided into shares. This type of company formation is resorted to chiefly when the company is an association without capital and carried on for purposes other than the making of profit. In unlimited companies, the liability of the members is not limited at all.

Incorporation of a public company.

Incorporation is essential in the case of a public company. Before a company is incorporated, the following documents will have to be filed with the Registrar of the joint stock companies:

- (a) Memorandum of association.
- (b) Articles of association, if any. In the absence of special articles, Table A attached to the Indian Companies Act, 1913, will come in force as the company's articles.
- (c) Notice of the situation of the registered office.

- (d) List of persons who have consented to be directors.
- (e) Consent of directors in writing to act as such.
- (f) Declaration by an advocate, attorney or pleader, entitled to appear before a High Court, who is engaged in the formation of the company, of compliance with all, or any, of the said requirements.

If the application is granted, a certificate of incorporation is issued, by which the company obtains a legal status. The company, however, cannot commence business or exercise its borrowing powers unless it obtains a further certificate from the Registrar declaring that the company is entitled to commence business. This is given when the following conditions are fulfilled:

- (a) Shares are allotted to an amount not less than the minimum subscription.
- (b) Every director has paid for on each of the shares taken or contracted to be taken by him, and for which he is liable to pay in cash, a proportion equal to the proportion payable on application and allotment on shares offered for public subscription.
- (c) filing with the Registrar by the Secretary or one of the Directors an application that the aforesaid conditions have been fulfilled and
- (d) in case of a company which does not issue a prospectus inviting the public to subscribe for its shares, there has been filed with the Registrar a statement in lieu of prospectus.

Two things need explanation here, viz., Memorandum of Association (M/A) and Articles of Association (A/A). To take up the M/A first, it is a document setting out the constitution of the company. Its object is twofold—first, that the intending investors of capital shall know in what field it is to be put; and second, that any one who shall deal with the company may know, without any doubt, whether the contractual relation which he contemplates entering into with the company is one relating to a matter within its corporate objects. In the words of Lord Macmillan, “the purpose of the Memorandum is to enable shareholders, creditors and those who deal with the company to know what is its permitted range of enterprise,

and for this information they are entitled to rely on the constituent documents of the company."

The contents of the Memorandum of Association are as follows:—

(a) Name clause, the name ending with the word "limited."

(b) Situation of Registered office.

(c) Object clause or nature of business.

(d) Liability.

(e) Particulars of capital—total amount of capital, number of shares, amount of each share and generally the different classes of shares. As the conditions imposed on a company by its memorandum can only be altered with difficulty, authority is frequently taken for a larger capital than the company wants immediately to employ.

(f) The Memorandum of Association must be signed by at least seven persons in a public company and two persons in a private company, who thereby become members of the company in question.

The essential characteristic of the Memorandum of Association lies in its unalterable character, which is thought necessary in the interest of the creditors, the outside public and the shareholders themselves. The Indian Companies Act expressly lays down that a company shall not alter the conditions mentioned in its memorandum except in the case and in the manner and to the extent provided for in the Act.

Thus a memorandum can be altered in regard to (1) name of the company, (2) the place of its registered office, (3) its objects, (4) its capital, (5) the rights attached to the different classes of shares and (6) the limited liability of its directors. A company may change its name by passing a special resolution and by obtaining the approval of the Central Government (by delegation, the Provincial Government). The new name has thereafter to be registered. Alteration of the place of registered office and objects can also be effected by a special resolution. But so long as they are unconfirmed by the court, the alteration does not take effect. As regards the alteration of the objects, the Act sets forth certain limits within which only any alteration is possible. They may be altered so far as it may be necessary

(a) to carry on its business more economically and more efficiently; or

(b) to attain its main purpose by new or improved means; or

(c) to enlarge or change the local area of its operation; or

(d) to carry on some business which under existing circumstances may conveniently or advantageously be combined with the business of the company; or

(e) to restrict or abandon any of the objects specified in the memorandum; or

(f) to sell or dispose of the whole or any part of the undertaking of the company; or

(g) to amalgamate with any other company or body of persons.

But any provision in the memorandum regarding the appointment of a manager, or managing agent and such other matters as are incidental or subsidiary to the main objects of the company can be altered without any special resolution, or approval by the Government or by the court.

To turn next to the A/A, if the memorandum of association is the fundamental document of the company, the articles constitute a subsidiary document, the purpose of the latter being to carry out the objects set forth in the memorandum. In case of conflict between the two documents or any part thereof, the memorandum will hold good.

The articles of association are regulations regarding the mode and form in which the business of the company is to be carried on and the internal affairs of the company as between the company and its members and its members and directors elected by them managed. The members are bound by the articles as if they, their heirs and legal representatives had signed them and had agreed to observe all the provisions of the articles, subject to the provisions of the Act. Any addition to, or modification of the articles can be made, subject to the provisions of the Act and of the Memorandum of Associations, by a special resolution. In other words, the alteration should not contain anything going against the law, should not go beyond the powers specified in the memorandum and should not

impose any additional liability on the members in the form of compelling them to take shares more than what they have already taken or to pay any more money than what they are liable to pay on their shares, without their written consent, either before or after the alteration is made.

Management of Public Company—Shareholders.

The position of shareholders in the management of a public company is too well-known to need a detailed discussion. In view of the number and type of persons in the list of shareholders and their wide geographical distribution, direct government of a public company by the shareholders is neither feasible nor desirable. Like the "common man" in a democratic form of government, the shareholder is not a specialist, whereas the management of a concern under present day commercialism has been so very complicated that it requires the wholehearted devotion of specialised brains. Nor has the ordinary shareholder time enough to bother on these matters. He has invested his money, not because he wants to participate in the management of the concern, nor because he is interested in a particular line, but because he has some money which he wants to utilise, but which he cannot do individually; so he has thrown it in a collective pool with an expectation of annual profit, which, he believes, will not be lower than the market rate of interest which his money would have fetched if deposited with a banker. Thus in a form of business organisation, where ownership is separated from management, the shareholder has become a passive recipient of income. The typical shareholder in modern business follows the sound principle of spreading the risk and owns holdings in a large number of different business undertakings.

The position of shareholders in India was all the more weak owing to the existence of the managing agency system. For this, however, the responsibility of the shareholders was no less negligible. In a country where, owing to the play of certain factors, which popularised investment in land or in ornaments or in government security, business investment had only a secondary and minor attraction, there could not be a strong class of investors in this country. Very few investors

who had invested had done so mainly because of their faith in the managing agency concern which stood behind the business, and not because of the soundness of the business itself. Naturally, these investors were limited not only to some industrial and business centres but also to a very narrow group of persons coming in intimate contact or having some blood relation with the particular managing agent. Thus since the investors invested their money not because of the soundness of the concern, but because of the particular managing agency firm, it was but natural for the shareholders to have their hands off business and leave the entire management of the firm to the managing agents, whose integrity had been the major determinant of investment. It is useless to go into the demerits of the system when no other course was feasible. In recent years, however, a tendency is visible for concerns being floated without the assistance of managing agents but simply with a board of directors. This, undoubtedly, is a tendency for the better; but yet, at this stage of our business development, we cannot say that managing agency system has outlived its utility when considered from the standpoint of business management. Whatever may be said against them on the score of specialisation, there is no denying the fact that these houses of managing agents have business in their blood and are far better suited than a body of shareholders and not less competent than a board of directors placed in direct management of a business concern.

The Indian Companies (Amendment) Act of 1936 has sought to strengthen the position of the shareholders, not so much, it seems, as regards their participation in the management of the concern, but in matters of their own rights. This is distinctly a step for the better. When business investment is coming to be more popular in India, anything that may trample the rights of shareholders—a possibility which is very great when the managing agents will find their hold loosened—would lead to its unpopularity. The rights of the shareholders, as recognised by the Act, are as follows:—

- (1) To have information that shares are allotted to them when they are so allotted.
- (2) To have within the prescribed time the share certificate.

(3) To have their names on the register of members, as also to have the register rectified, and in case of company's refusal to rectify, to apply to court for necessary relief.

(4) To transfer shares, subject, of course, to any restrictions imposed by the articles.

(5) To attend meetings, to receive proper notices and to vote at meetings of the company.

(6) To declare dividends and to apply to the court for an injunction restraining the directors from making payment of dividends on an *ultra vires* declaration or payment of dividend out of capital.

(7) To inspect registers kept by the company and to have extracts from it.

(8) To have copies of Memorandum and Articles, on request, and payment of prescribed fees.

(9) In case of a further issue of shares by their company intending to increase its share capital, the right of the existing members to have a first chance to buy new shares.

(10) To have statutory report, except in case of a private company.

(11) Where articles are not registered, the right to have, on request, copies of every special resolution passed by the company, to have also minutes of proceedings at general meetings.

(12) Their control over directors and managing agents and right to remove by an extraordinary resolution a director, appointed or elected, before the expiration of his period of office and the right to appoint, by ordinary resolution, another person as director.

(13) To approve assignment of office by directors.

(14) To approve by a resolution at a general meeting the appointment of a managing agent, removal of managing agent or variation of a managing agents' contract of management.

(15) A managing agent cannot assign or transfer his office unless the same is approved by members; and the members have also the power to remove a managing agent who is convicted of a non-bailable offence, in relation to the affairs of the company, punishable under the Indian Penal Code.

(16) Right to have a just balance of profit and loss account and to have the balance-sheet with the auditor's report.

(17) Right to apply for the appointment of one or more

competent inspectors by the Government to investigate the affairs of the companies.

(18) Power to appoint, by special resolution, inspectors to investigate the company's affairs.

(19) Right to appoint at the company's general meeting an auditor or auditors.

(20) Right to have a share in the capital of the company and in surplus assets, if any.

(21) To resolve by a special resolution that the company may be wound up by the court or voluntarily.

(22) To appoint and fix the remuneration of one or more liquidators in case of voluntary winding up and to fill up any vacancy in the office of a liquidator so appointed by them.

Side by side with the rights granted to the shareholders, there are also certain liabilities. They are as follows:—

(1) To take shares, when they are allotted in due time and in compliance with the provisions of the Act.

(2) To pay for shares allotted, when allotment is made and when calls are validly and in compliance with the provisions of the articles made.

(3) To forfeit or lose shares in case of non-payment, when a valid call is made.

(4) Liability as a member, even inspite of a valid transfer of shares, if the name of the transferee is not placed on the register of members, in lieu of transferor's name.

(5) Duty to abide by the doings of the majority of members unless the majority acts vindictively, oppressively, mala-fide or fraudulently.

(6) Their rights are liable to be altered or abrogated in accordance with the provisions of Memorandum and Articles, subject, of course, to the provisions of Section 66A which lays down that if the majority is oppressive or fraudulent, the minority of shareholders of not less than 10 p.c. of the issued shares can appeal to the court.

(7) Liability as a member in case the name of a person who has not agreed to be a member or is not or does not remain to be a member is allowed to remain on the register of members.

(8) Liability as contributory in case of winding up.

(9) Unlimited and several liability, even in case of a

limited company, in case the number of its members falls below the minimum prescribed as requisite number of members and the company does business inspite of such fact for more than six months after the number of members is reduced below 2 in case of a private company, or below 7 in case of any other company.

Management of Public Company: Directors.

The board of directors has long been regarded as an "anomaly" in business concerns in India. The reason for this is obvious. Since the managing agency firms have a great control over concerns financed by them, the directors, although formally appointed by the shareholders in general meeting, were the men of managing agents, depending for their continuance in office on the latter's favour. This being the case, the directors or the majority of them, were mere puppets in the hands of the managing agents who had in almost all cases the ultimate say in the matter. Since the Amendment of the Indian Companies Act of 1936, this hold of the managing agents has been reduced in so far as the managing agents can, except in case of private company, in no case appoint more than one-third of the whole number of directors. Thus the aforesaid "anomaly" has been substituted by a dual government—by managing agents by virtue of the finances advanced and by the board of directors by virtue of the powers given to them.

The appointment of directors is obligatory in the case of a public company and also in the case of a private company which is subsidiary of a public company. Usually the first directors are appointed by the articles of the company, the subsequent appointments being made by the members in general meeting. If the articles of the company do not appoint persons who are to act as directors, then, before the first directors are appointed by members in general meeting, i.e., during the intervening period, the subscribers of the memorandum are to be the directors. Casual vacancies in the board are to be filled up by the board itself, and the incoming director shall also retire along with other directors. Unless there is a provision in the articles or special contract to that effect, the directors are not entitled to any remuneration. But

they are to take up their qualification shares as prescribed by the articles within two months of their appointment or any shorter period so provided by the articles.

In the eye of law, the directors hold a dual position—*viz.*, directors as trustees and directors as agents. As trustees, the directors are to work in the sole interest of the company. In other words, they are not entitled to make any personal profit or obtain any benefit as against the interests of the company and, if they do so, in that case they are liable to make good the loss, if any, incurred by the company or to return the advantages secured by them. The directors are trustees of the money of the company and are jointly and severally liable for breach of trust. They have got discretionary powers as regards the allotment of shares, registration of transfer of shares, recommendation of dividends, etc. All these powers given to the directors are, however, to be exercised for the benefit of the company. As agents, the directors are to act on behalf of the company and to do all that the company can do. We know that a company is a legal person, having an existence separate from that of the members constituting it. The functions and powers of this legal person are to be exercised by the directors, for which, when acting *ultra vires* the directors are not personally liable, and they have every right to claim to be indemnified with regard to all acts validly done.

The powers of the directors are varied in character. They have the power to issue shares, to allot share, to refuse transfer of shares, to recommend dividends, to contract on behalf of the company and to bind the company by acts *intra vires*, to make calls in accordance with the articles, to accept full amount payable on shares or a part of such amount before calls are actually made for such payments, to forfeit shares for non-payment of calls, to accept surrender of shares and to set aside a part of profits as reserves. How very real these powers are, as compared to those of the shareholders, can be best illustrated with the help of one illustration. It is in the immediate, as distinguished from ultimate, interest of the shareholders to earn as much dividend as possible and, if allowed, by the weight of sheer majority, they can do anything. So the directors have been granted the power to recommend dividends, and the dividends declared by the company in general meeting

cannot exceed the amount recommended by directors. If they so think fit, they may not recommend any dividend but simply retain the undistributed profits, or carry them to a reserve fund or invest them in trustee securities or in any other bona fide securities as the company may think fit. If the profits of the company seem to justify it, the directors can declare an interim dividend. But then there is one restriction on the power of the directors, viz., that they cannot declare any dividend out of capital or otherwise than out of the profits of the year or any other undistributed profits. The payment of interest, in certain cases, out of capital, is provided for in Section 107 of the Indian Companies (amendment) Act of 1936. Thus, for instance, in the case of the Tata Chemicals Limited, the Government of Bombay sanctioned the period for payment of interest out of capital on the 5 p.c. cumulative preference shares upto 30th June, 1943 or the close of the half year next after the half year during which the works and buildings of the company were actually complete and the plant provided, whichever was earlier. The interest on preference shares had been paid out of capital at the rate of 4 p.c. per annum upto the 31st March, 1942, the remaining 2 p.c. cumulative to be paid out of future profits.

In the case of a winding up, however, a director cannot exercise his powers or act on behalf of the company, unless assigned by the Court or the liquidator or the general meeting of the company.

Turning next to the liabilities of the directors, the directors are liable for *ultra vires* acts, for breach of trust, for acting dishonestly, for negligence, for tort or fraud of co-directors and for wilful wrong or default. They are to vacate office, to retire in rotation, and may also be removed from office. They are also liable for mis-statements or concealments in a prospectus or a statement in lieu of prospectus, to be convicted under the provisions of the Act for non-compliance with the requirements of the Act and for unjustifiable delegation of duty and authority.

Generally speaking, the liability of the directors is limited to the amount remaining unpaid on the shares taken. But if the memorandum so provides, it may be unlimited; and even

if limited at first, it may be converted, if authorised by the articles, into unlimited liability, by a special resolution.

Side by side with the powers given, certain disabilities have also been imposed on the directors. In the first place, the directors cannot assign office to somebody else without the approval of the company by a special resolution. A director can, however, appoint a substitute or alternate director to act for him during his absence of not less than three months, provided the appointment of a substitute is permitted by the board of directors. Secondly, unless the company is a banking company or a private company which is not the subsidiary of a public company, no loans can be granted by the company to the directors. Thirdly, except with the company's approval, a director cannot hold any office of profit under his company, except, of course, the office of a managing director, a manager, a legal or technical adviser or a banker. Fourthly, a director cannot enter into contract with a company or a firm of which he is a director or a partner, without the approval of the board. And finally, directors cannot, except with the consent of the company, dispose of or sell away the undertaking of the company or remit any debt due by a director

CHAPTER IV

FORMS OF ORGANISATION (Contd.)

Rise of Combinations.

Perhaps the most noteworthy feature of modern business, not only in the field of production, but also in the field of distribution, is the increased scale of an individual unit and the growth of combination. In the earlier days of industrial and commercial revolution, too much emphasis was placed on free competition; of late, however, the wheel has turned in the opposite direction and free competition is making room for a system whose sole object is to restrict competition not only within the national frontiers but even in the field of international commerce. The evils of the trade slump have been another factor giving stimulus to combination. For, it is considered that during the bad days of depression, when the small firms will be swept away, a larger undertaking may continue to live on its own resources and may survive the crisis. Among other factors stimulating combination, mention may be made of the desire to control raw materials, to control markets and to avail of the economies of large scale production and distribution.

When the classical economists started any discussion, they invariably assumed one thing, *viz.*, prevalence of free competition. In "a world of monopolies" this sort of assumption had a boomerang effect and the theory of Economics became "an apparatus of the mind, a technique of thinking," without any further utility. In the present-day world, when combinations are to be found in almost every field, "monopoly is not a question of yes or no, but one of degree." In the words of Kalecki, "A world in which the degree of monopoly determines the distribution of the national income is a world far removed from the pattern of free competition. Monopoly appears to be deeply rooted in the nature of the Capitalist System: free competition, as an assumption, may be useful in the first stage of certain investigations, but as a description of the normal state

of capitalist economy, it is merely a myth." Here the word "degree" should be read with special importance. For the present-day organisations are neither wholly monopolistic nor wholly competitive. It is all a question of degree, beginning with informal agreement at the lowest stage to the consolidated form of organisation at the highest. The nature and extent of monopolisation also varies in different fields of business. Thus where raw materials and half-finished goods are concerned, a greater degree of monopoly is feasible; not so in case of finished goods. unless, of course, the source of supply of raw materials and half-finished goods, to be utilised in the production of finished goods, is also under the absolute monopoly of the concern in question and no substitute can be utilised for it. Otherwise, absolute monopoly becomes rare, and what Chamberlain has termed, "monopolistic competition" becomes the rule. To be a bit more clear, when a number of competing firms are producing one and the same thing, each one of them will try to produce at the competitive price but at the same time, though maintaining the same qualitative standard, try to make its product look a bit different, possibly superior, so that it may attract the "goodwill" of the customers. This device is very often supplemented by propagandist methods for the exploitation of the psychological weakness of the consumers.

In the field of economic theory, Sraffa's warning was very much timely, but the difficulty of theoretical formulation of the "degrees of monopoly" appears to be almost insurmountable. For, each business has its own technique and to strive to convert all the different enterprises into one formula will lead nowhere except to abstraction. Sraffa's efforts at analysis of monopoly "immediately swallowed up the competitive analysis without the smallest effort." The Robinsonian analysis, though aimed at a study of imperfect competition, does not lead us much towards reality: for, after all, it resolves itself into a study of the problem of demand and supply. And so far as the analysis of demand goes, it is concerned not with the demand for commodities coming from the ultimate consumers, but with the demand for "productive instruments and services." It may, of course, be argued that the nature and extent of demand for the productive instruments and services, in their

turn, influence the price of finished goods; but the process of imperfection, it must be remembered, does not end merely with the former type of demand, but also extends itself to the finished goods as well, as already noted. Thus her analysis becomes "highly abstract" from which it may appear "rash" to draw any conclusion applicable to the real world.

Whatever that may be, the question from the standpoint of business organisation is, whether, when the unit of control in business increases in size, there is any very considerable improvement in the technique of production and distribution? At this point, a distinction must be made between the advantages of big business and those of combination. A business may grow to an enormous size, far beyond the limit of requirements of the optimum firm, as, for example, the Madura Mills Co., Ltd., Madura, having 229868 spindles, although the average spindleage for the whole of India in 1940 was about 26000 and for the Bombay Island and Province was about 29000. The minimum required to ensure the cheapest cost of production was according to the evidence of the Bombay Millowners' Association to the Tariff Board, 30000 spindles. The case of Madura Mills Co., is one of big business, a result of expansion—a feature in business organisation which will be considered in a subsequent chapter. At this stage of our discussion, our sole concern is to consider whether, and to what extent, the expansion in the size of business leads to efficiency and economy. The difficulty in the way is no doubt very great and a detailed knowledge of the technical situation is called for before any estimate of the economies which may reasonably be expected from monopolisation can be made. At this point we must agree with Robinson when he says that "different types of monopoly hold out very different hopes of technical reorganisation. When a scheme takes the form of machine-wrecking, pure and simple, as in the case of the National Shipbuilders' Security, Limited, or of restriction of output by quotas without any concentration, as under the Coal Mines Act of 1930, there seems little reason to expect any increase in efficiency; whereas an organisation which exercises a detailed control over a large number of productive concerns may have very great possibilities of technical improvement."

While taking it for granted that different types of mono-

poly hold out very different hopes of technical reorganisation, let us next consider the nature and extent of the benefits derived from combination. In this respect, the verdict of a practical businessman who had promoted so many industrial consolidations in America, I mean, Charles R. Flint (*Memories of an Active Life* (1923), quoted by Mead, *Corporation Finance*) will be of immense help. Flint writes in his *Memories*:

"The most important benefit to be derived from it is the attainment of high-speed-automatic-machine-low-cost-standardised quantity production, which makes possible the manufacture and maintenance of products of superior quality.

"Because of the magnitude of their affairs, industrial consolidations are able to offer, in salaries and a percentage of net profits, generally over and above a previous maximum, a sufficient inducement to secure men of the first order of ability—men who are not tempted by a fixed salary, but by the incentive of making a record and profiting by it.

"The consolidated corporation, under a system of comparative accounting and comparative administration, subdivides its business so that each of its various departments are headed by a man who, through long experience and concentration, operates at the highest efficiency. Furthermore, industrial consolidations are able not only to secure the best men as executives, administrators and employees but also to retain men of the highest standing in the consultative professions—lawyers, engineers, architects, chemists and other advisers and technicians. Thus better service is assured, with an overhead cost less than the aggregate amount which was paid to men of lesser capacity by the various constituent companies.

"The consolidation not only adopts the best methods to be found in any of its various plants, but it improves them through continual experimentation by the ablest experts.

"It reduces stocks of merchandise, thereby saving interest and carrying charges and minimising loss from depreciation.

"It centralises sales and advertising and eliminates duplicate trade catalogues.

"It greatly reduces the volume of fixed and circulating capital per unit of output.

"It retains lawyers and experts of experience and demonstrated ability for patent and trade mark protection. By con-

solidation inventive genius is less hampered by conflicting patents and expensive litigation is largely eliminated.

"It utilises the advantages of a central traffic control, eliminating duplicating routes in the transportation of products sold and received, and locates factories with relation to labour, raw material and markets.

"Consolidation facilitates financing; the shareholders have greater security than they generally have in ownership of individual companies; their shares are available for loans, or convertible into cash and are readily divisible for the disposal of part interests or for sub-division by will."

This is a fairly wide catalogue; but how many of them are actually realisable and to what extent depends on the degree of monopoly prevailing in a country. But it gives a rough idea as to their nature and extent and there is no doubt that most of them are realisable and lead to efficiency and economy in a fully developed, or nearly so, monopoly. The most careful and penetrating research as to the efficiency of combination has been carried on in the United States of America by the National Industrial Conference Board for about sixteen industries over a period extending from 1920 to 1926. The method adopted was to measure the relation of output per worker employed in consolidations and in independent firms. It was found as a result of this investigation that out of sixteen industries, eleven showed a superior efficiency for the year 1926: Of these eleven, six showed a marked superiority and the improvement in the five, though not so great, was by no means negligible; even the remaining five were at an advantageous position over independent firms. Our assertion in a previous paragraph that a more perfect type of monopoly is possible in concerns producing raw materials or half finished goods is also corroborated by the investigation in question when it was found that the advantages of consolidation reached the maximum in metal refining and also in case of mineral manufacture. Even in matters of technical advance, consolidation has shown distinct advantage. Out of eighteen industries considered, technical advance was greater in case of consolidation in nine industries, in case of independent concerns in four and there was no significant difference in case of the rest. Thus the argument often advanced that in matters technical, monopolisation may lead

to "scrap heap" is falsified by American experience, and the conclusion arrived at is "that industrial consolidations have not impeded technical progress. On the other hand, they have been among the foremost leaders in experimenting with and introducing time-saving methods of production."

In matters of utilisation of existing plant and machinery also, combination seems to stand at a greater advantage over separate competing concerns. For, in so far as they can pool orders from various customers and know beforehand the nature and extent of demand, they can control not only output and prices but also can utilise the existing plant and machinery to the maximum extent and thereby reduce the fear of loss due to obsolescence which stands so heavily in present-day industrial world. This, to a great extent, reduces their capital requirements in so far as the fullest utilisation of a particular plant or machinery is possible before new installation is called for.

The problem of efficiency and management will be considered in a later volume. Suffice it to note here that the problems of management, though difficult and complicated, are by no means insoluble. In matters technical, the difficulties are exaggerated; for, in any concern, the technical work is nowhere infinite but is distributed among a number of units and in each unit there is further sub-division. The problem of co-ordination is of course there. But that too is not much difficult; for, sometimes the work of each unit is complete in itself. In those cases where co-ordination of technical work over the whole concern is to be undertaken, there is a certain limit beyond which the expansion of combination would, under certain conditions, be uneconomical. In matters of general management and financial control, co-ordination over the entire concern is necessary; to a theoretician this seems to be a difficult problem. But if we look at a concern like the General Motors in America, whose organisation comprises some eighty companies all branching out in unrelated lines, the aforesaid difficulties would seem to be exaggerated. On the authority of big businessmen we can say that there is no limit imaginable to which a business concern under proper guidance cannot go. (cf. Sergeant Florence: *The Logic of Industrial Organisation*.)

In matters financial, the claim very often put forward that monopoly facilitates economy in this matter also does seem valid to a considerable extent. So far as the shareholders go, the shares of a consolidated concern have a greater attraction in view of the stability of the concern. A policy of profit stabilisation can be more successfully carried out in the case of such a concern and this also raises them in the estimation of the investing public. As regards financial achievements of combinations over independent concerns, opinions, however, differ; but investigations in American business show that, though not absolutely, but from historical standpoint, combinations have, on average, achieved a greater success, from the beginning of the present century, over independent concerns and if the rate of progress is maintained,—and there is no reason why it should not—it will outstrip the independent concerns in near future.

Degrees of Monopoly.

In considering the degrees of monopoly, the scheme prepared by the Board of Trade for the *Balfour Committee*, and adopted by E. A. G. Robinson, distinguishes between three forms of organisation—short-term, transitional and long-term. But a hard and fast distinction on these lines of stability seems to be less scientific in view of the fact that what we term as short-term may actually prove to be long-term, whereas in a long-term form of organisation, trouble on any particular point may lead to disintegration. A more scientific approach would be to consider the different degrees of monopoly at any one time and different degrees at different times, the latter being, so to speak, an evolutionary process in the development of combination.

To consider the different degrees of monopoly at any one time, first, we should begin with what are known as “informal understandings or gentlemen’s agreements” between competitors as to the prices to be charged or the areas to be served, their effectiveness depending on the honour and faithfulness of the members. In this type, no formal organisation is to be found for regulating output or maintaining prices. But it has actually been found that although less formal, yet, actually,

they are more effective than the more formal type of organisation. This type of agreements whether conscious or unconscious, is very common in smaller trades. Sometimes the parties in question come to a formal agreement; but very often, without any such agreement, they may be charging the same price, particularly so, when price-cutting is to the advantage of none of them. The most familiar illustration is that of doctors' fees.

A slightly more developed type of business organisation is to be found in the simple agreements, also known as price agreements and trade agreements. In a simple agreement, there is an express understanding between the different business units not to control the quantity of output to be marketed, but simply to control prices, as happens in case of freight charges in shipping rings and conferences, in which case they are known as price agreements, or to control trade conditions, *e.g.*, terms of credit, methods of packing and shipping, dealing with competitive products, advertising, transport and labour, etc., in which case they are known as trade agreements. Trade agreements are very much common, in this country as in others, in the commercial organisation of the cities and towns, *e.g.*, the chambers of commerce, the Boards of Trade, etc. In the above two agreements, output is not controlled; but at times, either under stress of depression, or even in normal times, owing to the excess capacity of the plant installed, a restriction of output becomes essential. This sort of agreement works in two ways; either the common authority fixes the actual output to be produced by each concern or it asks the member concerns to work only a certain proportion of the plants installed, leaving the rest idle. Another form of simple agreement to be found is known as industrial price agreement. This type of agreement is concerned with the technical processes of production and seeks to maintain a level of prices which is not far too above the expenses to be practicable. Although a simple agreement, it may operate over a long period of time, may be closely and formally organised and may be local, national, even international, in scope and extent.

From the standpoint of organisation, members in a simple agreement, retain a large measure of individual identity, the object being, in general, merely to restrict competition rather

than to secure economies in production. Very often they are loose and informal types of agreement, with less or no publicity, but aimed at exploiting the public. Dissolution of this type of organisation may sometimes be necessary when they are acting in a way contrary to the public interest. Dissolution in this case does not cause much hardship in so far as the separate ownership and management of the properties is little affected by the agreement. But resort to dissolution should be had only in extreme cases; for, otherwise, when they are doing good to trade, e.g., trade associations striving to standardise the usages and practices, they should, under all circumstances be encouraged.

Another type of business organisation is known as Pooling Association. Here a distinction should be made between speculative pool and industrial pool. A speculative pool, which throws stocks into a common fund for the purpose of speculative operations on the exchanges and whose members share the pecuniary gains of these operations according to an agreed proportion, is temporary in character and exclusively concerned with profits won by artificial modifications of supply. This type of organisation does not interest us much. An industrial pool, on the other hand, is "a form of business organisation established through federation of business units whose members seek a degree of control over price by combining some factors in the price-making process in a common aggregate and apportioning that aggregate among the units." In this type of organisation, some degree of control over supply is essential and is exerted more or less directly. The "factor in the price-making process" is not the same in all cases. In one case, it may be output pool, in the other, territorial allotment or market pool, and in the third, income and profit pool. In the case of output pool, the object is to avoid overproduction and it therefore operates on the supply side. The members combine to the extent of making their output, form an imaginary aggregate fund or pool and then divide that pool among themselves according to some agreed basis. If a producer exceeds his production of the total output, he pays into the pool a sum proportionate to the excess, calculated on an agreed basis; any producer producing less gets a similar sum in proportion to the deficiency. Sometimes the fund is utilised

for subsidising export of the surplus product and thereby keeping national prices steady. In case of territorial allotments or market pools, the arrangement ensures a certain demand to each member; but this type of pooling agreement is very often found associated with output pool. In case of income and profit pools, these are pooled together in a common fund, and then distributed among the member concerns in proportion to the contribution of their output or at some agreed proportion.

A fourth type of organisation is association for allocating contracts. This type of organisation exists in those fields where work is allotted by tender. It is for the association to decide which firm is to receive a particular contract and accordingly it is arranged that other firms do not submit any quotation. Sometimes it so happens that if only a single tender comes, the purchasing authority may not accept the quotation and call further tenders from a wider field. In order to avoid this, other members of the association will also tender, but quote a higher price, so that the particular firm which, according to the agreement, is to get the contract for supply, is helped to obtain it. If a particular field is monopolised by a single concern, it is not rare to find the same concern quoting different quotations in different names. This is a single-concern association, if we may name it in this way. The association allocating contracts is to be found not merely within the national borders but are sometimes international. Thus E. A. G. Robinson notes the case of the British-American Tobacco Company as an international combine of this character. This combine co-ordinates in the export market the sales of the (British) Imperial Tobacco Company and the firms which before 1911 composed the American Tobacco Trust.

The form of organisation that is very much popular in Germany is the participating Kartell, its object being "to erect a dam which might check the destructive force of competition, and secure for a large number of businesses some place in the sun." The most characteristic feature of this type of organisation is that the competing producers agree to establish for a definite period a joint selling agency for the exclusive sale of their products, each producer being allotted a "participation" in the total output. The selling agency or syndicate is registered as a company, in which the individual producers are

shareholders with votes in proportion to their output. The base price is fixed by the members in such a way as to cover the cost of production and sell to the syndicate at an accounting price which is usually somewhat higher. The syndicate sells the product to the consumers at the highest price possible, adjusting its price to circumstances in different markets, though it does not as a rule sell below the accounting price. A slightly different form of kartell organisation is one in which the syndicate may acquire a considerable degree of independence or it may fall under the control of a particular concern or group of concerns. In this type, domination by one concern or a group seems to be more familiar. As for example, we may cite the case of domination of the German iron and steel trades by the Vereinigte Sthlwerke A. G., and of the German electrical industry by two concerns, the Siemens-Schuckert and the Allgemeine Elektrizitats Gessellschaft.

It is a peculiarity of the German industrialism that since its inception it is dominated by this kartell type of organisation. In their origin, many of these kartells were mere price agreements. In time, however, it was found that this simple organisation was not sufficient to attain the desired results over a period of time and hence they went further and regulated production. The first large scale organisation was formed in 1876-77 when an agreement was entered into by the Rhenish-Westphalian coal owners to reduce output by 10 p.c., the experiment being repeated several times during the seventies and eighties. In early nineties a selling organisation was also formed and by 1903 it controlled about 50 p.c. of the German coal output. There were many old and well-established kartells in metallurgical industries, *e.g.*, Pig-iron Syndicate, Fool-steel Kartell, and Kartells for rails, wire, half-manufactured steel, steel sheets and tubes. These kartells of steel trade formed in 1904 the Steel Union, which by 1911, consisted of 30 steel works.

The prevalence of kartell organisation in Germany evoked a very great discussion but no unanimity of opinions was arrived at either in its favour or against it. The adverse criticism came mainly from small industry, the main objections being that they were trampled by these bigger organisations, that they maintained prices at an artificial level, that they were

not satisfied till they had converted the merchants into commission agents and that they subsidised the dumping of goods abroad in order to keep the prices at home at a standard level. But when analysing the business organisation as such, we must note the following words of a devoted student of German industrialism. Thus Dawson writes in his *Industrial Germany*, "An impartial estimate of the syndicates and their operations requires the admission that they have achieved great results in the higher and more efficient organisation of industry, in the regulation of prices and of employment and in the more successful cultivation of the foreign market. These gains have not been unaccompanied by disadvantages to certain sections of the community as consumers, but as yet it cannot fairly be contended that the syndicates have flagrantly abused their powers, unrestricted though these powers are by law or by administrative measures."

Now, we shall consider some of the more permanent types of organisations. One such combination organisation is the Trust. Roughly speaking, the trust is any big monopolistic combination. But as a specific business form, it has a more definite meaning. The trust is "a form of business organisation established through temporary consolidation, in which the stockholders of constituent organisations under a trust agreement transfer a controlling amount of their stock to a board of trustees in exchange for trust certificates. These certificates show their equitable interest in the income of the combination. The trust differs from corporation organisation in this that it is a combination of business units. But, more than that, its legal attributes are quite different. Trustees are not as directors the paid servants of stockholders nor are they mere agents. They act as principals, making contract for themselves and being able to sue and be sued. The debts of the trust are not those of the beneficiaries but are the personal debts of the trustees."

The trust form of organisation is based on the mutual consent of the members who sign a "trust agreement". The net income of the constituent organisations is pooled and then paid out to certificate-holders in proportion to their interests therein, as evidenced by the certificates. In a trust, there is a transfer of the legal title to stock in the constituent concerns.

A formal organisation is formed to look after the trust. The trust is not a confederation but a federation—a more permanent type of business organisation—with an assured succession of trustees. The oft-quoted example of trust is the Standard Oil Company. This is truly regarded as a “lawyer’s device”, for, the legal obstacles in the way of a loose type of combination organisation were very great in America. So in order to evade the provisions of the law against combination, the trust form of organisation came into existence. Since the constituent concerns lose their separate existence, the whole organisation becomes a single one. Thus, on the one hand, it can evade law against combination and on the other it obtains a virtual monopoly in a particular line or several lines.

In the United States of America, the trust form of organisation was gradually superseded, after it had been declared illegal in 1892, by another form, known as Holding Company. Of all the more permanent types of business organisation, the holding company is by far the most common. This form of organisation is created for the purpose of combining other corporations by owning a controlling amount of their securities. This is, of necessity, the creation or prior existence of a corporation which has power to hold the securities of other corporations. The securities may be acquired either by direct exchange of its own securities or by purchase of securities of other companies. The ownership of the securities of various companies gives to the holding company the right to elect their boards of directors and to dominate their policy. The controlled corporations are nominally independent and operate under their own names, but they can be effectively managed by the holding company.

In its organisation aspect, it is more akin to a corporation than to a trust. For the holding companies issue stocks or shares, and not certificates as in the case of a trust. It has a board of directors, like any other corporation, and not a board of trustees. There is another difference still. In the formation of a trust, the stockholders of constituent companies surrender their stock to be held in trust for them by trustees. Thus they become mere beneficiaries of a trust agreement, having surrendered all control over management of the concern. Not so in a holding company. As already seen, the

corporation acquires a controlling interest by acquiring the shares of other concerns, the latter thereby becoming subsidiary concerns. A holding company has as its primary purpose the effecting of a combination which cannot be accomplished by the use of any one of the corporations which it is intended to include. Financial considerations also favour the use of this device. When the subsidiary companies are big enough, they manage their own finances; but when they are small, the holding company renders financial assistance.

The following types of holding company organisation have been noted by Haney. In the case of a consolidated holding company, it is formed by consolidating the existing enterprises. In the case of a parent company, the parent company is formed first and then it proceeds to organise subsidiary companies. A holding company may exist with holdings of all the shares of constituent corporations, or of a majority or only of a minority. A pure holding company engages in none of the technical processes of production directly but merely holds stock of subsidiary companies which are actually operating. The operating or mixed type engages in technical processes along with the holding of stocks. If the holding company is a primary one, it stands at the head of the combination organisation with no other organisation before or above; but in the case of intermediary companies, they are the agencies through which the primary company controls subsidiaries. There is another type of holding company, known as finance and investment holding companies, their purpose being not to combine competing organisations or those producing in different industries, but to promote financial operations and investment. Finally there are the manufacturing and transportation holding companies, the purpose of which is quite clear from their very names.

This form of organisation has distinct advantages over many others. In the first place, its principal advantage lies in the facility of promotion. Any attempt at outright purchase of any corporation would lead to severe opposition from the interested parties. The formation of a holding company requires no consent of shareholders. The would-be holding company goes on purchasing the shares of other corporations and when it has acquired a controlling amount, it becomes

parent company. On the score of capital, the holding company has greater advantage over any other corporation; for, it enjoys the advantage of being a combination, it has got greater claim to legality, a greater ability to appeal to investors through joint stock device and its limited liability are distinct advantages. In matters of management, unless in a trust, it can effect a unified central management and at the same time preserve some amount of individuality and initiative of the constituent concerns.

But then the powers of a holding company may be misused, as they actually were in the U. S. A. Thus this form of organisation enables the corporation to conceal from the Government and from public many matters which if expressed would not find public approval. This danger becomes all the more great because of the fact that the holding company possesses power without responsibility. Stock watering has been a very common feature of a holding company organisation and the innocent public have been duped on more than one occasion; in fact, the hope of gain through selling watered stock has been the chief object behind the formation of many concerns of this type. The most serious abuse of holding company organisation is to be found in the U. S. A. where many banks, immediately before the depression of 1929, were affiliated through holding companies with companies primarily dealing in securities, some being affiliated even with real estate companies. The abuses in the field of public utility were also by no means rare, and were followed by their control under the Public Utility Holding Companies Act of 1935.

There remains one more important type of combination, known as Consolidations or Mergers. This type represents complete combination, the merging of two or more businesses into a single undertaking. The combining companies entirely lose their separate existence. They may be of horizontal or vertical type. In the former, undertakings carrying out the same functions in a particular trade are combined, the chief object being the utilisation of the advantages of large scale production. Vertical combines are combinations of companies engaged in various stages of production of the article in question, the main object here being to avoid the vicissitudes of the market as regards raw materials or semi-manufactured

goods. It is interesting to note that the vertical combine is steadily going out of favour. In a period when violent fluctuation in prices is taking place, this form of organisation has definite advantages; but in normal times, as a result of combination, a concern may not be in a position to reap the full benefit of market conditions, should more advantageous terms be offered.

Leaving aside these major types of combination, there remain a few more which may, in brief, be noted. One such organisation is the Selling Agency. Unlike in a kartell, there is no control by the agency on the output. Only a number of competing firms agree to hand over their output to a common selling agency, the object being to prevent undercutting of prices. Another type of combination organisation is known as Community-of-Interest. Here, there is no formal central administration; but the business policy of the combining companies is controlled by a group of common shareholders or directors. Sometimes, the same directors are placed on the board of several concerns. In some cases the pooling factor is profits, which is, afterwards, divided among the combining companies in some agreed proportion. In theory, Community-of-Interest organisation is a temporary one, and the companies retain their separate existence and management. But it has been found by experience that there is often a tendency for this form of organisation to give way to a more complete union. This form of organisation with pooling of profits is a familiar feature of the German chemical trades.

We have considered degrees of monopoly at any given moment; there may also be degrees of monopoly over a period of time in which case the combination organisation is in a process of evolution. In this respect, no other country offers a better illustration than America. Prof. Ripley, writing about the year 1905, has distinguished four periods in the growth of combination movement in the U. S. A. The first period, covering the years from 1873-87, is characterised by an increase in the size and number of large scale organisations. Various pools were formed at this time in iron and steel business, in the distilling industry and in the manufacture of cordage; but the Standard Oil Trust foreshadowed the future development. Since the pools were a loose type of organisa-

tion, difficult to manage, there being no stability in prices, there was a quest for a better form of organisation. The second period, from 1887-97, is therefore mainly characterised by the formation of trust. The depression prevailing between 1893-97 put a check upon combination movement and some of the states came forward to render assistance. It was considered that financial combination would be of help and was therefore given legal sanction in some states. The holding companies originated in this way and was the most prominent type of business organisation between 1897-1904, when adverse law had been passed against trust. From 1904 onwards, the American business situation is characterised by a number of "speculative scandals." After the first world war, the movement has taken to new channels in which, as already seen, there is a branching out of a concern into unrelated lines. Thus the process of evolution is quite marked—from a less complicated type to a more complicated type and therefrom into branching out in different lines. In the Imperial Germany, some such evolution can be traced; but the disturbance following the consequences of the great war has checked the process of evolution, the whole structure being reorganised and rationalised according to the ideas of the particular administrations.

Combinations in India.

In India, combination has assumed, not so much the shape of evolution, as of organisation of combination in this line or that according to exigencies of circumstances. But the most familiar type that attracts our notice is financial integration as a result of the existence of the managing agency system. This integration has taken two forms—one, financial integration in the same line and the other, financial integration in different lines. The cotton mills of Bombay and Ahmedabad are an example of the first variety. In these two centres, a managing agency firm looks after several cotton mills, although in Ahmedabad the number of mills under a single managing agent is, as a rule, fewer than in Bombay. This type of combination resembles to some extent a horizontal combination,

though not so rigid and consolidated in character as the latter is to be found in the Western Countries.

Turning, next, to the second variety of financial integration, *viz.*, combination of firms in different lines under one managing agent, it may be noted that it resembles neither the vertical nor the horizontal type. It is of course true that under pressure from the managing agent, two firms working in the same line have combined together, as happened in the case of the Buckingham and Carnatic Company, Limited, Madras; but the problem does not end there and it is found that the same managing agent may have interest in some other lines. A list of some managing agents working in different lines is given below, which will give an idea of the number of undertakings under each firm. The list is not exhaustive but considers only a few important managing agency firms in this country. They stood as follows in the year 1942-43.

Name of Managing Agency Firm.	Rail way	Jute	Tea	Coal	Cotton	Sugar	Engine- ring	Misce- llaneous
Andrew Yule & Co	—	11	14	10	—	1	—	9
McLeod & Co. Ltd.	6	6	4	—	—	—	1	—
Martin & Co.	7	—	—	4	—	—	1	1
Dalmia Jain & Co. Ltd.	1	—	—	—	—	1	—	2
Jardine Skinner & Co.	—	4	5	1	—	—	—	2
Balmer Lawrie & Co.	—	—	—	1	—	—	4	3
Gillanders Arbuthnot & Co.	2	2	6	1	—	—	—	3
Shaw Wallace & Co.	—	—	6	6	1	—	—	2
Kilburn & Co.	—	—	7	3	—	—	—	—
H. V. Law & Co. Ltd.	—	—	—	5	—	—	—	1
F. W. Heilgers & Co.	—	2	—	6	—	—	—	1
Anderson Wright & Co.	—	1	—	2	—	1	—	—
Bird & Co.	—	8	—	2	—	—	1	5
Macneill & Co.	—	2	—	5	—	—	—	1
Karamchand Thaper & Bros Ltd,	—	—	—	1	—	1	—	1
Tata Sons Ltd.	—	—	—	—	4	—	1	2
Birla Bros. Ltd.	—	1	—	—	2	—	—	2
Kettlewell Bullen & Co	—	3	—	—	2	—	—	—
Killick, Nixon & Co.	—	—	—	—	1	—	—	1
Begg, Dunlop & Co.	—	4	10	—	—	—	—	—
Duncan Bros. & Co. Ltd.	—	1	24	—	—	—	—	—
James Finlay & Co. Ltd.	—	1	1	—	—	2	—	—
Begg Sutherland & Co. Ltd.	—	—	—	—	—	6	1	—

Some people have felt a confusion to explain this peculiar form of integration, because they say that they do not find

its prototype in any other country. That is of course true to some extent. But in certain respects it resembles the system prevailing elsewhere. Take, for instance, the new line of amalgamation movement in U. S. A. where the same concern is managing and financing so many different lines. And from the standpoint of the managing agency house, our system resembles that prevailing in Japan. In that country, financial power has been mainly concentrated in the hands of a few great corporations under the aegis of families, such as those of Mitsui, Mitsubishi, Yasuda and Sumitomo, to name the most outstanding of the families. They may compare very well with the Houses of Tatas and Birlas. It must at the same time be admitted that the concentration of financial power is not so very great in this country as in Japan. Thus the House of Mitsui in Japan controls above 25 p.c. of the paid-up capital, reserves, debentures and investments of all Japanese companies. In its main and subsidiary companies, the House of Mitsui is interested in such diverse activities as banking, insurance, trust business, transport of all kinds, warehousing, electric power and light, mining, textiles, metals and machinery, chemicals, manufactured goods, foreign trade, home trade, newspapers, forestry and plantation ownership. Behind all these diverse activities stands the Mitsui Bank with its capital amounting to 100 millions yen.

The circumstances leading to the ascendancy of the financial capitalist have been different in these two countries. So far as Japan is concerned, in the earlier stages of industrialism, government acted in the role of entrepreneur and after the concerns had stood on their own legs, they were handed over to the private initiative, which, of necessity, was represented by these big houses. Smaller industrialists were, of course, by no means rare. But in the years following the great war and particularly since the thirties, the great capitalists, using the financial institutions under their own control, have built up an ever-expanding complex of activities. In this country, owing to the political turmoil prevailing, no indigenous capital was forthcoming to trade and industry. A beginning was made in this respect by non-Indian firms in the eastern parts of India where they acted as company promoters and afterwards owners and financiers. In the cotton industry

of Bombay and Ahmedabad, Indian managing agency firms came forward. The financial capitalism started in this way and, it must be admitted, has played a very important role in the commercial and industrial development of this country.

The financial integration under the managing agency system has assumed diverse forms. Thus it has been found that surplus funds of a concern are often deposited with the managing agency firm at some rate of interest, the firm then having full discretion in the use of this money either in its own business or in another concern under the same managing agency. Sometimes these funds are permanently invested in allied concerns, and sometimes they are loaned on short-term accounts. Funds are sometimes raised on the credit of one concern and till they are actually needed or employed, they may be utilised for some other purpose by the managing agent, or lent to a concern under the same managing agency, other than that for which they were raised. Thus it was revealed at the time of the Tariff Board investigation of 1927 on cotton textile industry that the balance sheets of many mill companies in Ahmedabad contained large borrowings on the one side and large loans lent out at interest on the other. The practice tended to grow during the years of depression when the managing agents became busy over the protection of the concerns under them. Whatever may be said against this system from the standpoint of shareholders of sounder concerns and also from the standpoint of economic theory and conception of submarginal firm, it must be admitted that it was because of the managing agency system and financial integration arising therefrom that the cotton mill industry of this country was able to face the bad days of depression, but for which many a concern would have to be liquidated thus giving a great shock to the rising investing class in this country. It is easy to argue that "reserves of several well-established mills have in this manner been frittered away by binding them to others newly started by the same managing agents," but in a country and at a time when no sufficient funds are available from the investing public nor are there any institutions for supplying the long-term financial assistance to newly started concerns, this sort of financial integration, though not sound from the standpoint of sound company finance, is imperative in existing cir-

cumstances, and so long as the integrity of the managing agency system is not doubted, there is no scope for any apprehension in this type of investment. The merits and demerits of a system are to be judged from the results achieved and not simply from a principle that may have been formulated under some peculiar circumstances. And when we look to the years of depression, we cannot but say that the combination of concerns under the same managing agent has been of immense help.

Financial integration is not peculiar to the cotton mill industry alone; even in the jute mills, another very important industry of the country, this sort of integration is to be found. In one respect, however, the case of financial integration in jute mills differs from that in cotton mills in Bombay and Ahmedabad, *viz.*, that inter-company-investment in jute mills was undertaken as a result of the special resolution passed by shareholders in general meeting. This shows that even the shareholders realised the necessity and approved of the measure of inter-company-investment. Although no such special resolution is to be found in many cases, though none at all, in Bombay and Ahmedabad, yet to suggest that the action of the managing agents was arbitrary in character would go beyond the limits of propriety. In view of the closer personal relation of the managing agents in Bombay and Ahmedabad with concerns under them, and with the shareholders no necessity was perhaps felt for a special resolution.

This financial integration, in its turn, has led to a greater degree of co-operation among the different units than would have been possible had these concerns been under the management of separate boards of directors. Even then the degree of co-operation has not been sufficient in view of the development in this respect in Western countries and also in view of the exigencies of the circumstances prevailing since the depression. It is peculiar that when other countries were promoting a greater degree of co-operation in matters commercial and industrial, the Indian Companies (amendment) Act of 1936 incorporated provisions which were adverse to financial integration as prevalent in this country. Thus according to one provision, loans to managing agents of companies other than private companies which are not subsidiary companies of

public companies are forbidden. In the same way loans to or by companies under the same management is prohibited. Without the previous consent of the board of directors, given unanimously, the purchase by the company of shares, stocks, debentures or other securities of companies under the same managing agency is forbidden. The managing agency can in no case issue debentures and cannot invest funds of the company without the approval of the directors. Whether these provisions, apparently sound, would prove beneficial in actual operation, particularly in times of depression, only time can show. But it must be admitted that the efficiency of business management depends to a considerable degree upon the extent to which the persons in managerial position enjoy unhampered freedom to pursue a definite policy. The managing agency system has enjoyed a great advantage in this respect. In a country where no sufficient supply of managerial ability is available, and where no sufficient capital is also available, the managing agency system has supplied both and in matters administrative has secured a high degree of efficiency and integration. The system, in its administrative aspect, has led in many cases to group-purchase, group-sale and uniformity in working and administrative control. In matters financial, the smaller or newer concerns under the same managing agent have not faced any greater difficulty than the bigger ones, since in both cases, it is not their individual integrity and credit but those of the managing agent that have been the sole determinant. In the words of Lokanathan, "without any formal combination or amalgamation and without losing their independent legal and functional existence, these various units are enabled to realise some of the economies, if not of large scale production, of large scale organisation."

Having studied the most predominant type of combination in India, we should now devote our attention to combination or amalgamation in different lines which have arisen as a result of the exigencies of circumstances. To consider the field of banking first, here, although there are the "Big Five", *viz.*, the Central Bank of India, the Allahabad Bank, the Bank of India, the Punjab National Bank and the Bank of Baroda, like the "Big Five" in England, yet their development was not on the same lines as in the latter country. In England, the

rise of big five was the result of bank amalgamation and consequent concentration of resources in their hands, followed by the development of a network of branch banking. In India, however, the most noteworthy feature is the concentration of resources to a large extent in the hands of the "Big Five", side by side with the increase in the number of banks. The result has been that whereas in England, the amalgamation movement had swept away the inefficient concerns, in India, however, inspite of the concentration of resources in the hands of a few banks, the increase in the number of banks is going on and as a result of the war-time boom and liquidity in banking system, the development of banking, particularly branch banking, and its improper distribution, has gone so far that a period of depression and deflation, which would, of necessity, follow the war, unless timely measures are taken, would prove disastrous to banking business. For, by this time some of the mofussil centres seem to be oversupplied with banking facilities and there is little reason to expect that they would be adequately fed by the trade and commerce of the regions involved.

In this field, amalgamation has taken place only in a few cases. Thus in 1923, the Central Bank of India absorbed the Tata Industrial Bank. The Lloyds Bank absorbed in 1923 the well-known eastern business of Cox & Co., and of Henry S. King and Co. The Allahabad Bank has been bought out by the P. & O. Banking Corporation, which in its turn was purchased by the Chartered Bank of India, Australia and China. Leaving aside these three cases, there has been no amalgamation in this field worthy of name, while at the same time the need for co-operation among the Indian joint stock banks is very great. This is not only essential for the sound development of banking and also for making preparation to face any unforeseen crisis, but also for meeting the competition of exchange banks which are now in increasing measure taking to inland trade financing. This competition would increase in intensity in post-war years when the need for meeting the strong competition from well-established exchange banks would be very great. The Banking Bill that is before the Central Legislature aims at increasing the paid-up capital and reserve with a view to strengthening their position against

crisis. Now it is for the banks to combine and capture the inland and, if possible, foreign business, so that in post-war years they can hold their own against competition from foreign exchange banks. In this connection it may be noted that the *Central Banking Enquiry Committee* and the Foreign Experts associated with it suggested the formation of an All-India Bankers' Association, one of whose aims would be the laying down of principles and conventions calculated to prevent unhealthy competition; but the *Central Banking Enquiry Committee* was against the imposition of any restriction on the branch activities of the exchange banks nor did they take with favour the suggestion put forward by some witnesses of confining the activities of the branches of exchange banks to port towns. Whatever that may be, the suggestion did not materialise; but in changed circumstances of to-day and in anticipation of the developments that would take place in post-war years, it is high time for Indian concerns to consider and reconsider the question of co-operation, if not of amalgamation.*

The position in insurance business is slightly better. Many insurance companies have already amalgamated with a view to strengthening their position. The following list from *Indian Insurance Journal*, compiled by Roy in his '*Life Insurance in India*' is self-revealing:

Till 1927, there was no association of an all-India character in the field of insurance business. In that year the Indian Life Assurance Offices Association was formed. The Association immediately took up the question of payment of unduly high rates of commission to agents and of rebating and passed strong resolutions condemning both and suggesting to the member concerns to discourage these practices. It is interesting to note that the Insurance Act of 1938 has placed restric-

* Indiscriminate branch banking resulted in banking crisis recently in Calcutta and also Bombay. The only solution lies in affiliation, amalgamation and absorption. It is gratifying that the bankers, at least some of them, have grown alive to the need for amalgamation, but as yet amalgamation has not started as a movement, which it should if the banking system is to avoid any setback in difficult times which lie ahead. It is the duty of the newly-formed Bankers' Association to encourage voluntary amalgamation. If voluntary action fails, intervention may be called for in the greater interest of the economic system.

Amalgamation in Insurance Business

<i>Name of amalgamating company</i>	<i>With which company amalgamated</i>
1. Taj Insurance Co., Ltd., Lahore. ...	} Star of India Insurance Co., Ltd., Lahore.
2. Good Luck Insurance Co., Ltd., Lahore ...	
3. Indo-Asiatic Insurance Co., Ltd., Ajmer ...	} Free India General Insurance Co., Ltd., Cawnpore
4. Hindusthan Security, Allahabad ...	
5. Modern India Life Assurance Co., Ltd., Calcutta ...	} Aryya Insurance Co., Ltd., Calcutta
6. Searchlight Insurance Co., Ltd., Lahore ...	
7. Premier General Assur- ance Co., Ltd., Patna ...	
8. Jatiya Kalyan Insurance Society Ltd., Calcutta ...	} Federal India Assurance Co., Ltd., Delhi
9. Great Orient, Lahore ...	
10. Providential Insurance, Aligarh ...	
11. Unity Insurance, Lahore ...	
12. Glory of India, Lahore ...	
13. Great India, Calcutta ...	
14. Hindusthan Bima, Lahore ...	
15. Central Life, Lahore ...	
16. Equity Insurance Co., Ltd., Lucknow ...	} All-India United Assurance Co., Ltd., Lucknow
17. Agarwal Insurance, Ajmer.	
18. Victory Insurance, Lahore.	} Sunshine Insurance, Lahore.
19. Frontier Insurance, Peshawar ...	
20. Meenakshi Insurance, Madras ...	

<i>Name of amalgamating company</i>	<i>With which company amalgamated</i>
21. Central Mutual Life Assurance Society Ltd., Bombay	} Prabhat Insurance Co., Ltd., Bombay.
22. Prabhat Insurance Co., Ltd., Bombay	
23. Modern Insurance Co., Ltd., Bombay	} Forward Assurance Co., Ltd., Bombay.
24. Aryan Life Assurance Society Ltd., Bombay	
25. All-India Security Life and General Assurance Co., Ltd., Bombay	} Champion General Insurance Co., Ltd., Bombay
26. Great Peninsular, Madras.	
27. Genuine, Calcutta	} Worldwide Assurance Co. Ltd., Bombay.
28. United National Insurance Co., Ltd., Delhi	
29. Hukumchand Life Assurance Co., Ltd., Calcutta	} Bharati Bima, Benares. Aryasthan, Calcutta.
30. Ganesh Insurance Co., Ltd., Madras	
31. Hindusthan National, Lahore	} Sterling Insurance Co., Ltd., Delhi.
32. Universal Protector, Calcutta	
33. United Assurance, Calcutta.	} New Guardian of India Life Insurance Co., Ltd., Madras
34. Bengal Mercantile, Calcutta	
35. All-India Railway Men's Benevolent Fund, Nagpur	} Bihar National, Patna
36. Nag Insurance Co., Ltd., Nagpur	
	} Eastern National, Calcutta
	} Social Life Insurance Co., Nagpur.
	} Federal India, Delhi

<i>Name of amalgamating company</i>	<i>With which company amalgamated</i>
37. Social Life Assurance Co. Ltd., Nagpur	} Associated Insurance Co., Ltd., Nagpur
38. Forward Assurance Co., Ltd., Bombay	} Federal India Assurance Co., Ltd., Delhi.

tion on the amount of maximum commission that may be paid to agents and has made rebating illegal. A few years back the same Association tried to promote a Reinsurance Pool of existing companies. It was suggested that the companies would reinsure the excess over their retaining limit, which would be fixed for each company. This excess would be distributed among the remaining offices in the proportion of each remaining company's retention limit to the total retaining limit of the rest of the companies. This proposal, however, did not materialise owing to the unwillingness of the bigger concerns to re-insure with the comparatively weaker ones and also because of the lack of standardised rates and policy conditions.

Turning next to the extractive industry, *viz.*, coal-mining, the need for combination here is very great. This aspect was specially emphasized by the *Coal Enquiry Committee (1937)* in their report. The committee has clearly shown how lack of co-operation is definitely working against the interest of coal trade. In the words of the committee, "voluntary restriction of output, with agreed-in minimum prices, has failed to materialise because the coal trade cannot combine even for obviously mutual benefit, while compulsory restriction of output, with authoritatively fixed minimum prices, has been rejected by Government. Consequently as a matter of economic necessity, production costs have been reduced to the subsistence or survival level, repairs and renewal of plants are limited to the lowest point compatible with safety and efficiency, depreciation cannot be provided for adequately and new developments are comparatively rare." How very inadequate this amalgamation has been can be understood from the following list of a few amalgamations: —

Amalgamation in coal mining.

<i>Year.</i>	<i>Name of amalgamating company</i>	<i>With which company amalgamated</i>
1939	Girimint Coal Co., Ltd.	Bengal Coal Company, Ltd.
1919	Bhaskajuri Coal Co., Ltd.	Burrakur Coal Co., Ltd.
	Central Jherria Coal Co., Ltd.	
	Jumoni Coal Co., Ltd.	
	Lutchipore Coal Co., Ltd.	
	Nowaghur Coal Co., Ltd.	
	Reliance Coal Co., Ltd.	
	Teetulumuri Collieries Ltd.	
	Bankola & Joba Collieries (by Purchase)	
1940	Aldip Coal Co., Ltd.	Equitable Coal Co., Ltd.
	Bansdeopur Coal Co., Ltd.	New Bansdeopur Coal Co., Ltd.
1920	Damuda Coal Co., Ltd.	New Beerbhoom Coal Co., Ltd.
1932	New Kendah Coal Co., Ltd.	

Not only there was no adequate amalgamation of concerns in coal mining, on the contrary, between 1914 and 1923 the number of coal mining concerns increased in India by 322 or about 50 p.c., while production rose from 16 to 20 million tons. This in itself is sufficient evidence of the fact that a large number of small companies came into existence during this period and increased the precariousness of the coal trade. In England the tendency was in the reverse direction and the number of coal mines was steadily reduced from 2861 in 1927 to 2075 in 1935, the majority of the mines closed being small ones. The result of the rise of these small companies in India has been the "fragmentation" of bigger mines some of which are "leased out in small strips involving great waste of coal in barriers, in-

creasing the danger of fire spreading from one property to another and generally making safe and economical working impracticable." The *Coal Enquiry Committee (1937)* was so much impressed by the waste involved that it recommended that "the Statutory Authority should be empowered to arrange voluntary amalgamations if possible and then proceed to compulsory amalgamation if the owners will not come to terms."

In the coal trade, since the passing of the Coal Grading Board Act of 1925, a sort of forced "trade agreement", if we may say so, has come into existence, not so much for standardising any trade practice as under a trade agreement, but for standardising the product.

The story of the salt trade from the standpoint of combination is one of domination and rate war by a combine of certain foreign concerns. The activity of this association is confined to the Eastern Provinces of India, particularly in the Calcutta market, in view of the fact that the Eastern Provinces of Bengal, Bihar, Orissa and Assam are, for climatic reasons, unable to produce sufficient salt and have therefore to depend on import. Even as early as 1903, the introduction of salt was followed by a noticeable reduction in price. A similar thing was repeated when the Indo-Aden Works first commenced to import salt towards the end of 1911; for, the price of Liverpool salt came down from Rs. 71/- to Rs. 41/- for 100 mds. Attempts at excluding the newcomers from the salt trade and to stabilise the prices at a high level have often been followed by informal agreement between manufacturers or importers and sometimes formal associations have also been formed, as e.g., in 1911 and 1918. A third combine came into existence in 1927 and is known as the Salt Importers' Association of Bengal. It comprised as its members the following concerns:—

- (1) The Salt Union of Liverpool, through its agents, M/s. Turner Morrison & Co., Calcutta.
- (2) The Union Salinera de Espana of Barcelona, through its agents, M/s. Turner Morrison & Co., Calcutta.
- (3) The Societa Italiana per le Saline Eritree of Rome, through its agents, M/s. Turner Morrison & Co., Calcutta.
- (4) Hamburg Salt Interests, through their representatives M/s. Lionel Edwards Ltd., Calcutta.

(5) The Port Said Salt Association, Ltd., through its agents, M. Grezoux, Calcutta.

(6) Augustine Burgarella Ajola of Aden, through its agents, M/s. Grahams Trading Co., Ltd., Calcutta.

(7) Indo-Aden Salt Interests, through their agents, M/s. A. & J. Lalljee, Calcutta.

The immediate effect of the formation of this combine was to maintain prices at an unduly high level throughout 1927 and for the greater part of 1928. Meanwhile the situation so far as the indigenous production of salt was concerned, had slightly improved owing to the granting of temporary protection, though at cautious rate, and the Indian producers urged, in a conference held at Simla, that if protection was continued over an adequate period, they would be able to supply the Indian market. This was too much for the Aden interests who started a fierce rate-cutting war, which was followed by dumping of East African Salt by Italy. It is peculiar that the Government also reduced the import duty at this juncture with the result that the Indian industry was on the verge of total collapse in 1933. Hardly a comment is necessary on Government policy. Ultimately in 1935, on an old recommendation by Tariff Board made in 1930, a Salt Marketing Board was formed, composed of Indian and Aden producers, the object being the elimination of foreign imports and regulation of Indian imports. For studying the fluctuations in the trade for co-ordinating supply and fixing the quotas, a Control Committee was formed. Slightly less than 50 p.c. of the quota went to the Aden group and the rest to the Indian group of producers. Thus the whole trade was divided between two groups of producers on the basis of quotas fixed by the Control Committee.

The oil industry of India is dominated by a combination, known as the Kerosine Pool, which in its turn is dominated over by one concern, *viz.*, the Burmah Oil Co. The Pool consists of the following companies:—

- (a) The Burmah Oil Company.
- (b) The Royal Dutch Shell Group.
- (c) The British Burmah Petroleum Company.
- (d) The Assam Oil Company.

In accordance with the maximum price policy of the

dominating company 1,95,000 tons of inferior oil, contributed by the member concerns at some agreed proportion on the volume of production of each concern, is sold to the Pool at a fixed price. The price paid by the Pool to the contributors is fixed every six months on the basis of following factors:—(a) current price f. o. b. American Gulf Port, (b) transport charges, (c) import duty, (d) profit at 10 p.c. on (a) and (b), and (c)-storage. This oil received by the Pool from different contributors is mixed before sale and then sold at prices which will cover the price paid to the contributing companies, but at the same time maintaining difference between the prices of inferior and superior quality of oil. Thus the object of the Pool is twofold—to mix the supplies of inferior quality of oil and sell it and to fix the price for this oil at a level which is profitable. The Pool, and in fact, the dominating concern, *viz.*, the Burmah Oil Co. have so great an influence that even concerns which stood outside the pool, *viz.*, the Standard Oil Co. and Indian concerns, like Indo-Burma Petroleum Co., have also followed the price fixed by the Pool. For, so far as the Standard Oil Company was concerned, the factor of distance as to the sources of supply, and so far as the Indian concerns were concerned, the negligible proportion of their output, made competition with the Pool impossible and brought them into line with the Pool.

Now we shall pass over to some of the manufacturing industries of India in order to see how far combination as a form of business organisation has affected them. To take up the premier industry of India first here, leaving aside the financial integration already studied, amalgamations in proper sense of the term have not been very many. Some of them can be seen in the following chart:

It is interesting to note that when the post-war boom gave way to slump, the leading mill agents in Bombay considered the possibility of amalgamation. A scheme also was prepared. The Tariff Board of 1932 gives the following description of the scheme. A scheme for the reorganisation of the industry in Bombay on the lines of the Lancashire Cotton Corporation was put forward by some of the most prominent mill-owners in the city early in 1930. Under this scheme no less than 34 mills under 7 managing agency firms were to amalgamate with the object of:—

Amalgamation in Cotton Mills.

<i>Name of amalgamating company.</i>	<i>With which company amalgamated.</i>
Ahmedabad Jubilee Spinning & Mfg. Co., Ltd. (by purchase) ...	Ahmedabad Manufacturing and Calico Printing Co., Ltd.
Kaiser-i-Hind Woollen, Cotton & Silk Mills Co., Ltd. (by purchase) ...	
Coral Mills (1924) ...	Bangalore Woollen, Cotton & Silk Mills Co., Ltd.
Tinnevely Mills (1927) ...	
Pandyan Mills (1929) ...	
	Madura Mills Co., Ltd.

- (i) standardisation of products;
- (ii) reorganisation of qualities so that single types or ranges of yarn or cloth might be allotted to individual mills;
- (iii) concentration of purchase and sale by single well-designed units;
- (iv) avoidance of duplication of work; and
- (v) elimination of uneconomic machinery.

Each mill was to be valued and taken over by the merger corporation at its current price paid in ordinary shares; its unsold stocks were to be paid for in cash and nothing was to be paid for goodwill. The control of the corporation was to be vested in a Board of Directors with working committees to carry out the following duties: —

- (a) purchase of cotton;
- (b) sale of yarn cloth;
- (c) purchase of machinery & stores;
- (d) management of mills;
- (e) arrangement of finance; and
- (f) organisation of research and statistics.

The corporation was to be financed by a loan from the Imperial Bank of India to the full extent of its liquid assets and by debentures. The project, however, did not materialise, possibly because it was "too ambitious a venture". But it is

interesting to note that joint action between some mills on certain matters has been possible and has proved beneficial. The *Bombay Textile Labour Enquiry Committee* in their Report (vol. II) have noted some of them. Thus, for instance, the Bombay Millowners' Association was able to secure a reduction in power costs from .725 of an anna per unit in 1926 to .35 of an anna in 1939, as a result of negotiation with the Tata Hydro-Electric Agencies, Limited. The Association also succeeded in organising the insurance of risks arising out of the application of the Workmen's Compensation Act (1923) through the Millowners' Mutual Insurance Association, Limited, which has now, after meeting all claims, accumulated a fairly considerable surplus fund. Substantial savings have been made by Ahmedabad mills as a result of a joint purchase of machinery in 1931-32. Leaving aside these matters, the cotton mill industry has not seen any amalgamation. The amalgamation scheme already noted did not find favour either with the Tariff Board of 1932 which was of opinion that better results were likely to be attained by economies accruing from close personal attention, or with the *Bombay Textile Labour Enquiry Committee* which was too much obsessed by the considerations of economic unit; but in the changed situations of the post-war years, when there will be acute competition from the British cotton textile industry, some such scheme of amalgamation would be not a matter of choice but one of necessity. It is no use arguing that the Bombay cotton textile industry is imbued with the spirit of individualism; for, this spirit cannot be of greater intensity here than that in Lancashire at one stage. If for self-protection, Lancashire had found it necessary to form a Cotton Corporation, the necessity is all the more great in India, not only for protecting the home market but also for retaining the new markets in Asia and Africa.

Although combination has not characterised our cotton mills, yet it cannot be said that they have been perfectly free in this respect. A sort of vertical integration is to be found throughout the whole country except in Madras. Thus in the reports of the Tariff Boards reference has been made to the marked increase in combined spinning and weaving establishments as compared with mills equipped for spinning only.

During 1931-1935, the former showed an increase in number from 231 to 265, while purely spinning concerns fell from 58 to 44.

If amalgamation in cotton textile industry was only a paper plan, in jute mills there has not been even such a thing. But in one respect, the jute mills are better situated in view of the fact that the working conditions for all of them have been determined from time to time by a central organisation which has a sufficient hold on the industry. In considering the different types of combinations, we remarked that experience has proved that simple agreements are more permanent than so-called permanent combinations. The validity of this assertion is well-proved by the working of the Indian Jute Mills Association which started its career in 1886. From time to time, the member mills,—and almost all mills except the Hooghly and Serajgunge were members—entered into agreement for restriction on hours of work—not in consideration of labour welfare, but for adjusting supply to market demand—and closing down a certain percentage of the looms. The agreement was renewed according to the situation. Thus, for example, by an agreement operating from October, 1931, the mills in the membership of the association, comprising some 95 p.c. of the trade, worked during 1932, 1933 and the greater part of 1934 for 40 hours per week, with 15 p.c. of the total complement of looms sealed. At the same time it was agreed that the mills would not instal any extra productive machinery or relative buildings during the currency of the agreement. Similar agreement was again entered into in 1936, with certain relaxations as to the hours of work in view of the changed situation. The agreements referred to applied only to member mills. In 1932, the Association entered into agreement with five principal mills outside the Association, *viz.*, Adamjee, Agarpara, Gagalbhai, Ludlow and Shree Hanuman, whereby these mills undertook to restrict their working hours to 54 per week up to 30th June, 1933. With certain modifications this agreement was extended and became a continuing agreement, being ultimately terminated in 1936. Whatever that may be, it is clear that the aim of this simple combination is to restrict the output of member mills in such a way as to maintain prices.

Unlike in cotton and jute industries, the paper industry

of India is characterised by a greater degree of combination. The policy of the mills belonging to the Indian Paper Makers' Association and also of those working in conjunction with it has been to combine for the purpose of price fixation and for the allotment of contracts with the Central and Provincial Governments, which represent 20 to 25 p.c. of their total production, according to an agreed arrangement among themselves. This combination was facilitated because upto recent times there was a practical monopoly of the trade between the three older mills, *viz.*, the Titaghur Paper Mills Co., Ltd., the India Paper Pulp Co. and the Bengal Paper Mills Co. The new mills that have of late come into existence have either joined or are co-operating with the Association. The combination has enabled the mills to maintain prices at a level slightly below the level of prices quoted for imported paper of similar quality; this has also enabled them to prevent the cutting of rates below an agreed level.

A greater degree of combination characterises the sugar industry of India. When we consider each independent concern, we find the existence of vertical combination in this industry. Some of the concerns not only manufacture sugar but also possess the supply of raw material, *viz.*, sugarcane, in so far as they have their own fields. Thus, for instance, the Buland Sugar Co., Ltd. conjointly with the Raza Sugar Co., Ltd., owns a subsidiary concern, *viz.*, the Agricultural Company, Rampur, and owns and operates an extensive light railway system in Rampur State which facilitates the supply of sugarcane to the factories. The Agricultural Company has also developed a separate sugarcane plantation, which is connected with the mills by the light railway system. Some of the mills have their own distillery. Thus the Cawnpore Sugar Works Limited have a gur refinery, and a distillery where country spirit, denatured spirit, rectified spirit and commercial alcohol are manufactured. All the more remarkable is the organisation of the Deccan Sugar and Abkhari Co., Ltd., which combines also the distributive side of trade. It owns a sugar mill and distillery in Madras where palmyra jaggery is refined and various kinds of portable and non-portable spirits are produced. The factory does not crush cane. A confectionery is attached to the sugar factory and a carbonic acid gas

collection, purification and compression plant adjoins the distillery. The company has a large number of agencies, sub-agencies and depots along the Coromandel Coast and inland for the purchase of palmyra jaggery and sale of sugar, spirit and other products. Other examples of vertical combination in sugar industry may be cited, but we have taken the most representative examples.

So far as the sugar industries of U. P. and Bihar are concerned, the Sugar Syndicate represents a central organisation for them. When the industry was passing through a crisis the organisation was formed by the Indian Sugar Mills Association to assist in the carrying of stocks over the remainder of the season. The fixation of minimum selling limits and quotas of supply for 92 factories which had joined the syndicate had the effect of steadying the prices. Be it noted that this organisation was formed to meet an emergency which had faced the industry. It is essential that some such organisation should be made permanent not only in the sugar industry but in other industries as well wherever there is the danger of overproduction as compared with the existing and to some extent, potential market. (Cf. the recommendations of the *Bombay Textile Labour Enquiry Committee* regarding cotton industry) and in order that it may be successful, it must have, direct or indirect, support from the Government (Cf. the following observation of the *Tariff Board* (1938) on sugar industry: "We understand that the first central selling organisation formed in Java in the year 1918 known as the United Sugar Producers' Association failed on account of a similar lack of co-operation and the eventual defection of some of its members. In 1932 the intervention of the Government was necessary for the formation of a new organisation.")

The cement industry of India presents the most perfect type of horizontal combination. The formation of the combination was the result of protracted experimentation. The industry which was in infant stage in 1914 expanded to a considerable extent as a result of the great war but was all on a sudden faced with competition, particularly from the United Kingdom, as a result of which, it was in a state of impending collapse by 1924. The hesitating attitude of the *Tariff Board* facilitated the refusal to grant protection by the Government

to this infant industry and many firms collapsed. However, as a measure of self-protection, the surviving firms formed the Indian Cement Manufacturers' Association in 1926. The first step taken by the Association was the fixation of selling prices; in all other respects, including sale and obtaining of maximum possible business for itself, each firm was fully autonomous. The Association also organised a joint sales service, called the Concrete Association of India, in order to educate the public and also to provide free technical aid as to the uses of cement. The year 1930 saw the establishment of a Cement Marketing Company of India, the object of which was to take over the control of sales and distribution for almost all the manufacturing companies in its membership, these companies working on a system of quotas based on the stated capacity of each company. These organisations were to some extent successful, but the constitution of the Marketing Company presented some difficulties. Even the quota system did not work smoothly and "it was often necessary to transport cement from one particular factory to an area which would have been more economically served from another factory near the area." Hence a complete fusion was favoured and effected in 1936 when the Associated Cement Companies Limited came into existence. The Associated Cement Companies took over by amalgamation the business and assets of the undernoted concerns which went into voluntary liquidation:

- (1) The Indian Cement Co., Limited.
- (2) The Katni Cement and Industrial Co., Ltd.
- (3) Bundi Portland Cement Limited.
- (4) The Akha Cement Co. Ltd.
- (5) The Gwalior Cement Co. Ltd.
- (6) The Punjab Portland Cement Limited.
- (7) The United Cement Co. of India Ltd.
- (8) The Shahabad Cement Co., Ltd.
- (9) The Coimbatore Cement Co., Ltd.
- (10) The Dewarkhand Cement Co., Ltd.
- (11) The C. P. Cement Co., Ltd.

Thus the rise of the cement merger in India is simply the result of the threat of foreign competition and unsympathetic attitude of the government. It is interesting that the dictum

that "Tariff is the mother of Trust," so much true in America, has been falsified in the case of the cement industry in India.

In miscellaneous industries, there are occasionally traces of combination. Some idea of the same can be obtained from the following chart:

Amalgamation in miscellaneous companies.

<i>Year.</i>	<i>Name of the amalgamating company.</i>	<i>With which company amalgamated.</i>
1928	Hukumchand Electric Steel Works ...	Bhartia Electric Steel Co. Ltd.
	British India Iron & Steel Co. Ltd. ...	
	...	
1936	Bengal Iron Company Ltd. ...	The Indian Iron & Steel Co. Ltd.
	...	
1920	The Cawnpore Woollen Mills Co. Ltd. ...	British India Corporation Ltd.
	The Empire Engineering Co. Ltd. ...	
	Cooper Allen & Co. Ltd. ...	
	The North-West Tannery Co. Ltd. ...	
	The New Egerton Woollen Mills Co. Ltd. ...	
	...	

Upto this time we have said nothing regarding the match industry which represents the most obnoxious type of international combination, *viz.*, the Swedish Match Company. Before the first great war, the Indian market was being supplied by Japan, Sweden and some other European countries. During the war years, Japan became the principal supplier of matches but had to yield position to Sweden after the war. The Indian factories numbering 21 in 1928 produced about 12 million gross a year. The Indian factories received some stimulus from the imposition of high import duty in 1922, but it was short-lived in view of the fact that the Swedish match company jumped over the tariff wall by the establishment of

factories. Thus while Japan was eliminated from the Indian market partly as a result of the import duty of 1922 and partly because of the amalgamation of some Japanese concerns with the Swedish Company, the Indian concerns stood face to face with this powerful international combine and the Tariff Board knew no method of recommending protection because "In our fiscal law there is no express provision which recognises the method of penalising unfair competition except where such competition arises from the payment of bounties." India was ill repaid when as a result of rate-war and the most objectionable sort of propaganda carried on by the Swedish concern against the Indian manufacturers as a class, a large number of Indian companies had to close their doors. An idea regarding the concern can be had from the following programme for bringing the Indian match industry in its grip: (From Adarkar's *Indian Fiscal Policy*).

"(i) The Western Indian Match Company (only a different name for the Swedish Company) has been nominally re-floated as an Indian public limited company with rupee capital. The capital is largely Swedish and the control is entirely Swedish too, except that the company has accepted a couple of Indian directors on its board.

"(ii) The Swedish Company has strengthened its position by expanding its output capacity with great strides. The company had in 1928 only 4 factories in India, but now it owns eleven factories in addition to the Indian factories which it controls indirectly by holding a large proportion of the capital.

"(iii) Negotiations have been and are being carried on, under duress of a ruthless rates war, with Indian factories, with a view to control and restrict their activity.

"(iv) The company has controlled the supply of Swedish and German match machinery through its subsidiary, *viz.*, the Match Manufacturing Supply Company.

"(v) A rates war which was initiated even before the *Tariff Board Enquiry* of 1926-28 has been steadily ruining the Indian Factories. The undercutting of prices has been such as to leave practically no margin of profit to Indian manufacturers."

Nothing can be more pitiable than this. Tariff has indeed proved the mother of distrust.

No less obnoxious to the interest of Indian trade is the combination of shipping serving—rather dis-serving—Indian trade. The combination in shipping is known as Ring. As a result of rate-war, the first shipping ring was formed in 1875, consisting of the Peninsular and Oriental Company, the British-India Co., and some other lines of London; George Smith and Sons and the City Line of Glasgow; Rathbone Bros. and Co. and T. & J. Harrison of Liverpool. The shipping Ring has stood not only in the way of development of Indian shipping whose share in the oceanic trade is scarcely 2 p.c. but it has also hampered our trade. The preponderance of foreign shipping even in the coastal trade of India has made the situation all the more precarious. As the Fiscal Commission pointed out about more than 20 years ago, the great disparities of rates between the charges on goods shipped from one Indian port to another and those on goods carried between India and foreign countries handicap Indian goods in transmission in comparison with goods from and to foreign countries. This is due to the fact that the steamship companies belonging to different countries grant numerous facilities to the export houses belonging to their own country and it is all the more tragic that the greater part of Indian foreign trade, as will be seen later, is in the hands of non-Indian export houses.

So far we have studied different industries in order to see how far they have been affected by combination as a form of business organisation and to what extent combination has proved beneficial or otherwise to Indian interest. Now we shall consider another form of combination for which the definition has been given by the Indian Companies (Amendment) Act of 1936, I mean, holding company. It should not, however, be expected that this form of combination is very wide in India. Unless, of course, we regard the managing agency firms holding a large proportion of shares in many concerns as holding companies, we cannot say that this form of combination has become very important in India as it has become in America. However, samples of this type are to be found in some industries.

The Indian Companies (Amendment) Act of 1936 has defined a holding company as follows: If a company's assets consist in whole or in part of shares in another company or

association so that the amount of shares held by it in that other company is, when accounts are made up, more than 50 p.c. of the issued share capital of the other company, or is such amount as would entitle it to have more than 50 p.c. of the voting power in the other company, or if it has power to appoint the majority of directors of other company, it is known as a holding company and the other company is known as a subsidiary company. The shares held by holding company may be held directly or through a nominee. A company may be a subsidiary company of another subsidiary company.

Now let us take some concrete cases of holding company arrangement in India. In the field of Railway, the Bengal Provincial Railway Company Ltd. owns all shares of Dasghara-Jamalpurganj Extension. In the same way, all the shares of the Darjeeling Himalayan Railway Extensions Co. Ltd., are held by the parent concern, the Darjeeling Himalayan Railway Co. Ltd. In the coal mining concerns also, holding company arrangement is to be found. Thus the Burrakur Coal Co. Ltd. became the proprietor of the whole of the shares in Loyabad Coke Manufacturing Co. Ltd. and also became the principal shareholder of the Sijna (Jherriah) Electric Supply Co. Ltd. Between December 1938 and August 1940, the Equitable Coal Co. Ltd., acquired a large majority of shares of the Aldip Coal Co. Ltd., by the exchange of 35735 ordinary shares of Rs. 10/- each, at a premium of Rs. 15 per share. In cement industry, the Associated Cement Companies Ltd. hold the greater part of the share of the Patiala Cement Co. Ltd., the entire share capital of the Cement Marketing Co. of India Ltd., and 40 p.c. of the shares of the Burma Cement Co. Ltd. In the last mentioned instance, however, the A. C. C. cannot be regarded as a holding company, since it holds less than 50 p.c. of the shares.

In the field of distribution, *i.e.*, trade proper, we have already noted the existence of a central selling organisation in sugar and cement industries, the latter resembling the selling syndicate in some features. Leaving aside those stray cases, this aspect is dominated upto this time by individualist spirit. Trade agreements, as already defined, are however, not rare. These concerns in India may be divided into four groups. They are:—

- (1) Chambers of Commerce.

- (2) Commercial Associations.
- (3) Planters' Associations.
- (4) Trade Associations.

(1) The objects and functions of some of the leading chambers of commerce may be noted. The Bengal Chamber of Commerce is an association of merchants, brokers, shop-owners, bankers, insurance companies and others. An important branch of its work is the measuring and weighing of most of the principal commodities exported from Calcutta. The Bengal National Chamber of Commerce was started to aid and stimulate the development of commercial and industrial enterprises in Bengal, to protect the interests of all persons trading therein and to promote unanimity and uniformity of practice among the members of the trading community. One of the functions of the Bombay Chamber of Commerce, performed through a Measurement Department, is the measurement of exports in the docks prior to loading. The Madras Chamber of Commerce was founded in 1836 with a view to watch and protect the interest of trade, to receive and collect information on all matters of mercantile interest bearing upon the removal of grievances and the promotion of common good, to receive references on matters of custom or usage in doubt or dispute, deciding on the same and recording the decision made for future reference and so form by that and other means a code of practice whereby the transactions by all engaged in it may be simplified and facilitated. The Mysore Chamber of Commerce has been recognised by the government as competent to issue certificates of origin. The Buyers' and Shippers' Chamber, Karachi, was started to safeguard and promote common commercial interests of the Indian Maritime Traders in particular.

(2) The commercial associations are mainly concerned with each particular type of commerce, as the names of the associations indicate: Blanket and Shawl Traders Association, Calcutta; Calcutta Grain, Oil-Seed and Rice Association; Calcutta Hides & Skins Shippers' Association; Indian Engineering Association, Calcutta; Indian Sugar Mills Association, Calcutta. Bombay Millowners' Association; Bombay Piece-goods Native Merchants' Association; Ahmedabad Millowners' Association, etc., etc. It should not, however, be thought that

all members belonging to the particular trade have become members of the particular association representing it. In a strong well-kint organisation like the Bombay Millowners' Association, most of the cotton mills have become members; for they realise the advantages of group action, in which the association has a long record of success. Individual employers or trades may have remained outside these associations, either because they are sufficiently confident in their own ability or because they are very small and negligible and may have refused to fall in line with the policy adopted by these bodies. Compulsory membership would however do no good; but, for specific purposes, *e.g.*, uniformity of trade practices and usages, etc., compulsion may be called for, if, say, the association represents a certain proportion of the membership of the trade. In industries like cotton mills, which have cropped up not only in different parts of India but also in native states, some all-India Association, federating the local associations together, may be of immense help in the matter of adoption of uniform working and trade conditions, particularly in native states, where these conditions, owing to the lack of adequate labour legislation, are rather lax.

(3) Planters' Association: The Indigo Planters' Association, Bihar, was formed as early as 1801 to facilitate correspondence with the government in the interests of planters, to safeguard their interests and to deal with applications for the settlement of differences. The successful exploitation of synthetic indigo has driven out many of the planters to some other agricultural occupations and hence the name of the association was changed into Bihar Planters' Association, Ltd., in 1905. The United Planters' Association of Southern India (Incorporated), Coonoor, was started with a view to promote and protect in all parts of the world the interests of various planting authorities carried on in Southern India, the collection and dissemination of statistics and information and settlement of differences by arbitration. The Indian Tea Association is also one belonging to this category.

(4) Trades Association.—These are concerned with trade proper. Thus in the Calcutta Trades' Association, membership is confined to retail traders, whether individual, partnership or joint stock company. The Calcutta Import Trade

Association was formed to encourage and secure united feeling and action amongst importers and generally to promote and protect the interests of those engaged in the import trade of Calcutta. One of its main objects is the fixation of points of customs and adopting of uniform forms of contract. The Bombay Traders Association was formed with the object of promoting and safeguarding the interests, general or particular, of the trading community in Bombay Presidency and also of collection and distribution of such information as may protect members of the association from loss or damage likely to arise in whatever manner. It undertakes arbitration when called upon to do so, collects debts due to members and acts as trustees on their behalf for liquidation, by persons indebted, of debts due to them. The Madras Trades Association was founded with the object of promoting the interest of the trading community of Madras, of furthering the adoption of a more healthy system of trade with reference to credit and of obtaining, as far as possible, accurate information of the position and movements of those dealing with or indebted to its members. It undertakes arbitration when necessary, collects debts due to the members and generally acts as trustees for the liquidation, by persons indebted, of debts due to them. All questions relating to hours of business and the fixing of holidays are dealt with by the Association.

Social Control of Business.

At a certain stage in its development, social control of business remains not a matter of choice but becomes a matter of necessity. This is true even in countries with so-called *laissez faire* tradition. This, it must be admitted, is due to certain diseases of industrialism and commercialism; but the diseases are not of the same type for different occupations in different countries at different times. They vary according to the stages in the development of industrialism and commercialism. The diseases in the earlier stages are entirely different from those in more developed stage, and the remedies, therefore, must, of necessity, be different in character and application. Power has a natural tendency to concentrate; and financial power is no exception. But this financial power,

leading to combinations and monopolies or coming in their wake, though associated with many economies of financing, production and distribution, is not altogether innocent of abuses that sometimes affect so many different classes of people as investors, labourers, and consumers. Different countries have, therefore, devised measures for the prevention of these abuses.

So far as the exploitation of labour is concerned, that constitutes a chapter by itself and we shall consider the matter, in brief, in connection with our discussion on labour and efficiency in another volume. The case of exploitation of investors and consumers is no less important and has attracted the attention, more or less, of those in charge of administration of the country. The efficacy of some of these measures may be questioned, and rightly, and it may be urged that even after ten years after the passing of the *Sherman Anti-trust Act* in U. S. A., the legislation was not successfully enforced. But then, partial or total failure in the enforcement of a law should not be made a plea for inaction. One thing must, however, be noted. The social control of business in a capitalist world where, with the rise of the new industrial and commercial class, its hold on the concrete expression of social authority has been predominant, the adoption and enforcement of measures for the purpose in view have at times been discouragingly slow, a process all the more intensified in India owing to the big gulf that separates the interest of the administration with those of the rank and file. But whatever that may be, here we are not contemplating about a social and political structure other than that in which we live and move and therefore we take everything as given.

As already pointed out, the intensity of the problem is not the same in all countries. Take the case of Britain. In that country till the years following the first world war, monopoly did not become a power in true sense and even at this period there were many industries, great and small, in which combination has hardly made any headway. In the field of banking, the rise of Big Five caused some disturbance and it was apprehended that if the process continues, it will give rise to a banking trust, more powerful than the Bank of England. It is interesting to note that although the investigating committee

suggested measures for enactment against further amalgamation, they were never enacted, but at the same time no amalgamation has taken place in that field without the approval of the Treasury. Where social co-operation of this sort exists, social control assumes a secondary role. In certain matters, as in coal industry, combination was encouraged, while in others, *e.g.*, cotton industry, production was restricted. Special arrangements were made for the encouragement of export of British products and the Empire Marketing Board did a lot in this respect. Above all, came the triumph of Imperial Preference at Ottawa. Thus, in brief, control in British industry and commerce was aimed at their further expansion and development. Social control of business in the interest of consumers has not assumed much importance in Britain. In the years following the great war, mention may be made of the Food Council formed in 1925 on the recommendation of a Royal Commission. But in the absence of statutory powers, it was not able to achieve much.

Social control of business has characterised the economic history of the U. S. A. The drive against monopoly in the interest of consumers started as early as 1890. In its legal aspect it was so rigorous that combination even in export trade was rendered illegal and this had to be relaxed with the change in situation after the first great war. But so far as the internal economy was concerned, public feeling, even in 1914, was so widespread that more rigorous legislation was desirable. Since the depression, the social control of business in America took a different turn and the crisis in banking was followed by rigorous banking legislations aimed at safeguarding the interest of depositors.

In India since commercialism and industrialism are in primary stages, the social control of business as understood in America has not started as yet. Besides, monopoly interests are so few that wherever a combination has taken place, it has been the result of self-protecting measure rather than a trust protected by tariff walls. Where self-protection is the guiding factor in combination--as we have seen in the case of cement industry--combination is followed by cheapening of products and efforts at their popularisation. Even in the case of other industries, like coal industry, need for combination is very

great in the interest of economy in working costs and also in the greater interest of consumers. In those industries where owing to the prevalence of the spirit of individualism, e.g., cotton industry, combination, though necessary, is not yet possible, some measure of common action has become absolutely essential in the changed circumstances of to-day. Only in cases like match industry, abuses have taken place and should be removed. Thus, far from saying that social control of business should include in its programme measures against combination, we must say—and it is backed by our analysis of conditions in combinations in India—that in certain fields at least, combination should be encouraged by direct or moral support of the government. This necessity to-day is the greatest in the field of banking.

Whatever may be said against the policy of the Government of India, no one can say that apparently they have been blind to the interest of consumers. All their policies of inaction and half-action have been justified on the ground that the teeming millions of India need the cheapest goods for their subsistence, from whatever sources they may be available and the theories of absolute and comparative costs in international trade have been of immense help in their formulation of policy. The whole idea behind "scientific" protectionism has been the interest of the millions of agriculturists in India, any sacrifice on whose part for the industrial development of the country has been deemed too much. Industry and trade have suffered, no doubt; but the agriculturist has got cheap goods. To-day, under the stress of war and post-war conditions, the consumer feels that he has been cared for too much and the policy of the Government in matters of industry and trade and their negligence of the distinction between the short-run and long-run interests of consumers have cost the consumers innumerable sufferings and privations. The Smithian School of Economists in India who had sung in praise of discriminating protection and *laissez faire* may feel a bit perplexed; but the man in the street asks: Is it social control of business?

Social control of business in India has taken another form; viz., control in the interest of shareholders. We have already seen how disabilities have been imposed on the managing agents and how the rights of the shareholders have been

strengthened. But we know that shareholders are sleeping partners; so in their interest audit of the company's accounts is compulsory in every country including India. As agents of shareholders, the auditors have power, if they are dissatisfied with the information or explanation given by directors, or if they find that the balance sheet does not represent the true position of the company, to report the matter to the members and to qualify their report on the balance sheet. The law has also made some provision in the interest of the would-be investors. It is well-known that the prospectus is the invitation to the public to subscribe to the shares. In order that the innocent public may not be duped, the law has clearly mentioned the details which should be revealed in the prospectus, a copy of which must be furnished to the Registrar before it is issued. So far as the declaration of dividend is concerned, certain restrictions have been imposed by law, *e.g.*, it will not exceed the amount recommended by the board of directors and it will not be paid out of capital; but in matters of capital structure of companies other than banking companies, there are certain weaknesses, *e.g.*, too wide a gap between authorised capital and paid-up capital, the ignorant public being duped by the former, which need handling in the interest of shareholders.

In the case of banking companies, the provisions are more far-reaching. Thus managing agency system has been abolished in their case, except when the managing agent itself is a banking company, but even then the banking company cannot be entitled to any remuneration, commission or share in profits. In order to save the shareholders from being duped by a big authorised capital it has been provided in an amendment to the Indian Companies Act, passed in 1944, that the subscribed capital of the company will not be less than half the authorised capital and the paid-up capital will not be less than half the subscribed capital. In order that a banking company may not be burdened by borrowed money, the amendment also provides that the capital of the company must consist of ordinary shares only, or ordinary shares and such preference shares as may have been issued before the commencement of the Amendment Act of 1944.

But more important is the interest of investors in the case of banking companies. In their interest also there are certain

provisions in the company law with a view to ensure stability. Section 277 of the Companies Act requires every banking company to create a reserve fund by transferring to the said fund out of the profits of every year and before any dividend is declared a sum equivalent to not less than 20 p.c. of its profits, until the amount of the said fund is equal to the paid-up capital of the Company. The said amount shall be invested in part. Govt. Securities or in Securities referred to in Section 20 of the Indian Trust Act of 1882, or keep it deposited in a special account to be opened in a scheduled bank. Every banking company shall also maintain by way of cash reserve in cash, a sum equivalent to at least $1\frac{1}{2}$ p.c. of its time liabilities and 5 p.c. of its demand liabilities. The Amendment Act of 1944 provides that notwithstanding anything contained in Section 103, no banking company shall commence business unless shares have been allotted to an amount sufficient to yield a sum of at least Rs. 50,000/- as working capital and unless a declaration verified by an affidavit signed by directors and the manager to that effect has been filed with the Registrar. All these provisions safeguarding the interest of shareholders and depositors form part of the Companies Act. The need for a separate banking law was felt long ago and was stressed before the *Central Banking Enquiry Committee*. It is gratifying to note that already a Banking Bill is under consideration which when passed, would be, it may be expected, more far-reaching in character from the standpoint of shareholders and depositors.

As in the case of banking, so in the field of insurance, a greater degree of control has penetrated, the only difference being that insurance business is governed by a separate Act. To prevent the formation and growth of insurance business by mushroom companies, the Insurance Act of 1938 provides for registration of all companies and a substantial initial deposit of Rs. 50,000/- in securities to be raised to a total of Rs. 2,00,000/- within a stated period. The investment of funds has been restricted and provision has been made for investment of not less than 55 p.c. of the life fund and the liability for matured claims, less any deposits made to the superintendent under the Act and loans granted on policies maturing in India and within their surrender values, in the following manner:

25 p.c. in Government Securities and a further sum equal to not less than 30 p.c. of the said sum in Government or approved securities, or securities of, or guaranteed as to principal and interest by, the Government of the U. K.

Combination is associated with two other problems for which, also, social control of business becomes necessary. These problems are, first, the distribution of productive resources and, second, uneven distribution of wealth. In the present stage of industrial and commercial development, none of these problems have assumed any mentionable significance. In advanced countries social control in the shape of planning or "comprehensive socialisation of investment" is essential for realising the maximum possible utility by reducing wastes to a minimum. In our country, of course, we cannot say that there is no mal-exploitation, rather than maldistribution, of productive resources, owing to the prevalence of foreign capitalism in most lines. But yet, in the infant stage that we are, our planning should be in the nature of proper utilisation of available and potential resources for the maximum possible benefit of the children of the soil. As regards the second problem, it must be said that it is neither peculiar to combination or monopoly nor to a particular country but to the present system. But since we have accepted the present system as it is for our purpose, ways and means must be devised for reducing this evil of uneven distribution of wealth. But then there is need for caution and what is sauce for the gander must not be regarded as sauce for the goose in these matters. Taxation as a remedy is well-suited, but where industrialism and commercialism are in infant stage, too heavy a rate of tax may break the camel's back. Some economists have gone so far as to suggest the abolition of corporation tax and modification of undistributed profits tax in India. While total abolition of the tax may give unnecessary inducement to declare fat dividends, a better step would be if an alternative provision is incorporated which may stimulate institutional saving, to be invested in the further expansion of the industry and trade.

CHAPTER V.

FORMS OF ORGANISATION (Contd.)

Rise of Co-operation.

The rise of co-operation as a form of business organisation marks a definite reaction against the present system. The evils of present-day industrialism induced the great minds to think over their solution. Of these, the revolutionary ones contemplated the overthrow of the present order of things. How far they were correct is a matter outside the scope of present discussion. We are concerned here with another group—and a less revolutionary one—which sought to remedy the evils within the existing structure. Experience has, however, shown that this type of business organisation has a very limited field for its operation and outside that field it hardly offers any remedy against these evils.

The word “co-operation” may be used in a loose and also in a restricted and proper sense. Loosely speaking, it includes any type of co-operation and cannot therefore exclude combinations that we have discussed in the previous chapter from its scope. Thus understood, it entirely loses its significance. Not only that; as a form of business organisation, some co-operative associations will hardly be found to differ from some forms of combination. But then if we forget the distinction, we will be going against the very purpose for which co-operation was thought over. In case of such a resemblance, the distinction is to be discovered not in its express organisation but in the spirit underlying it and it is this spirit that distinguishes co-operative organisation from any other type found so far.

The literature on co-operation is so exhaustive and the definitions given are so many that one finds himself perplexed. The reason is that the organisation has assumed different forms in different occupations and in different countries, with the result that each writer in formulating the concept is influenced by the peculiar circumstances around him. Some writers have

sought to consider all the definitions available, both in theoretical formulation and statutory enactments, and then have tried to find out a definition by taking the common elements in them; but this process of averaging is no better. In arriving at the restricted and proper definition of the word, a negative approach is more fruitful and scientific. What, then, are the evils of industrialism that have led to the rise of co-operation? Broadly speaking, they are twofold—in the field of production and in that of distribution; and the worst sufferers are the labourers, both as actual producers and as consumers. Co-operation is therefore a sort of joint enterprise by the workers both in the field of production and distribution with a view to reduce to the minimum the evils of the existing system of production and eliminating middlemen and their profits in the field of distribution, each member sharing in the profits, earned at a nominal rate, in proportion to his contribution to production and to the use that he makes of the association in distribution. Some writers have emphasized “poverty” and others weakness as the main reason for the rise of co-operation; no doubt, they are partially correct. But the main reason is the feeling of injustice and reaction resulting therefrom. Consider the matter calmly. What is co-operation for? Undoubtedly, it is for remedying the evils of existing system—a halfway house, so to speak, between capitalistic exploitation and socialistic utopia. If therefore the labourers are to take over the existing system of production and distribution in their hands, they must have sufficient capital not only for initial financing but for continued working as well. And it is well-known that modern productive and distributive machineries require enormous capital. If co-operation is an organisation of the “weak” and of the poor, it is something entirely different from that envisaged in the above lines. Co-operation is no less distorted than socialism in the hands of capitalist writers.

It is discouraging however that co-operation as a form of business organisation has attained a very negligible success in the field of distribution and almost no success in the field of production. The only field where it has attained a certain degree of success is co-operative store. Otherwise, it has remained a weak men’s and poverty-stricken men’s association. This no doubt is a “mighty fall”; but one thing is clear, *viz.*, that

co-operation is no panacea for the evils of modern industrialism and commercialism.

In India, the co-operative movement was introduced not for remedying aforesaid evils but as a solution of the poormen's problem. This is all the more evident from two facts, *viz.*, that co-operation in India was not the result of spontaneous growth but an official imposition and that the first enactment on co-operative societies in India, the Act of 1904, was based on the English Friendly Societies' Act of 1896. In view of this, the success attained is all the more limited. We shall discuss the nature and extent of Co-operative Societies in India in connection with our discussion on retail trade. In this chapter, we shall simply concentrate our attention on the organisation of a co-operative society in this country.

Co-operation as a form of Business Organisation.

We have already remarked, as a form of business organisation, co-operation has not attained anything remarkable, unattained by any other type of business organisation. Even in a country like England, where the store movement has made great progress, it is only a form of retailing—one among many. The legal position of co-operation is a story of continuous evolution. Under the Friendly Societies' Act (1793), only friendly societies formed for thrift and providence by working classes for pooling their small resources for friendly relief and mutual benefit were registered. Societies formed for trading purposes, like stores or producers' societies could not be registered under the Act. In 1846 a slight advance was made when a clause was added to the Act which provided "for the frugal investment of the savings of the members for better enabling them to purchase food, etc. But still a serious handicap remained in so far as the activities of these societies were restricted to members only. The Industrial and Provident Societies' Act of 1852 authorised the formation of co-operative societies and gave all the advantages obtainable under the Friendly Societies' Act. The Amending act of 1855 enabled the societies to hire or purchase land and in 1862 a new act was passed by which limited liability was allowed to co-operators; trade could henceforth be carried on, except banking and

mining. Henceforth the profit could be applied for any purpose permitted by law, a member could invest in a society upto £200, and for the first time, the certificate of registration constituted the society a body corporate and the shares of one registered society could be purchased by another registered society to the maximum limit of £200. The Act of 1867 removed this last limitation and brought the working of mines and quarries within the authorised purposes of the society. By an amendment of 1871 the societies were allowed to erect cottages and other buildings, to buy and sell them and to advance money on mortgage and other securities. By the Act of 1876 the societies were allowed to undertake banking business. The whole law was consolidated by the Industrial & Provident Societies' Act of 1893.

Prior to 1904, there was no special law in India governing co-operative societies. These societies, could be formed under the Indian Companies Act but could not enjoy any special privileges; they were on the same legal status and had to submit, if registered, to the same restrictions as any other concern registered under the Act. If they were not registered, they could not enjoy the rights given by law to a registered company, nor could they expand in size without registration, for, under the Act, any association carrying on banking business with more than ten persons as members was regarded as "illegal" association. Like a joint stock company, a co-operative society is also an association of persons; but in so far as the object of these two types of associations is not the same, one being profit-earning and the other for mutual benefit, the control of both the associations in the same manner stands in the way of the encouragement of the latter type. The situation improved with the passing of the Co-operative Societies Acts of 1904 which recognised only the credit aspect and of 1912 extending the provisions to the non-credit societies formed on co-operative basis, thereby laying down "the fundamental conditions which must be observed" and giving "such societies a corporate existence without resort to the elaborate provisions of the Companies' Act."

In the case of a joint stock company, the object of its formation is to be clearly mentioned by the company under the "Object Clause" in the Memorandum of Associations. The

company cannot go beyond the objects thus mentioned in its working, without a change in the clause through special procedure prescribed therefor. It is therefore not rare to find concerns having a wide range of business as objective, though actually they take to one or a few of them at the outset. In some countries like America, there is already a liberalising tendency as a result of which, in the words of Cook (quoted by Hoagland: *Corporation Finance*.), "Public policy does not require business corporations to confine themselves strictly within the limits of the words of their charters." In India although this liberalising tendency is not visible, yet the practice of including a wide range of objectives in the Memorandum is not rare. In the case of a co-operative society, the intended objects are included in the bye-law. Here also in order to avoid the necessity of altering the bye-law or of establishing a new society for a different object, the practice in some countries is to have a wide range of objectives in the bye-law, though most of them are not availed of at the outset. So far as the Indian Law of 1912 is concerned, there is no restriction on any combination of objects for the furtherance of the economic interests of the members. Thus although the law is quite extensive, situational restrictions have stood in the way of its expansion and whatever success has been achieved, has been achieved mainly in the field of credit—and there too, the *Bombay Banking Enquiry Committee* reported that the share of the co-operative societies in financing agriculture "is considerably smaller than that of the *sowcar* and the *quasi-sowcar*", and the *Assam Banking Enquiry Committee* reported that "so far as we can see the exploitation of cultivators by the village mahajans...by village money-lenders...ex-tea-garden coolies and others is on the increase."

A casual observer of the co-operative movement in India will realise that the Registrar of the co-operative societies is the very foundation of the movement. Apparently, he has been vested with a very wide range of powers, nay, duties, much wider than that entrusted to the Registrar of joint stock companies. Whether this official domination has been a success is a much disputed question among the writers, although from the results achieved, the verdict leaves no scope for hesitation about the conclusion. In the literature on co-

operation, one group is urging that "the popular movement should be handed back to the people" and that "state controlled co-operation...will hardly offer a permanent solution towards our endeavour to build up a vigorous and self-reliant movement," while the other group, while admitting the necessity of de-officialisation, points out that the time for the same is not yet ripe because "co-operation...is not spreading by its own momentum." The Government officials point out that "the control of the movement by official Registrars has been a success, and has not in any way tended to paralyse progress." We have already hinted the results achieved so far after forty years of fostering care and this inadequacy is mainly due to the fact that since the Government is there, the co-operators have never taken the matter seriously and considered the society as anything different from any other Government agency. Whatever that may be, some of the provincial legislation has, instead of reducing official control, passed further measures to strengthen it and in this respect no part of India has been so progressive as Bengal which has "enacted a comprehensive piece of legislation for co-operative societies, the general effect of which is to strengthen the control of the Registrar as well as the financing bank over the co-operative societies—of the financing bank through power to direct amendment of the bye-laws and of the Registrar through power to dissolve and reconstitute the managing committee as well as to depute an official or other person to manage the affairs of the society." No more comprehensive officialisation has ever been devised than this. Indeed, "India has been saved many failures and many years' delay by the present system" (Calvert); but it has not paved the way of progress. If stagnation is the goal, that has been partially achieved.

There are certain conditions which must be satisfied before a society may be registered. Unless the Local Government otherwise directs, a society which has as its object the promotion of the economic interest of its members in accordance with co-operative principles, or a society established with the object of facilitating the operations of such a society, may be registered under the Act with or without limited liability. No society, other than a society of which a member is a registered society, shall be registered under this

Act which does not consist of at least ten persons above the age of eighteen years and where the object of the society is the creation of funds to be lent to its members.

The main obligation of registration is the keeping of proper books and the presentment annually of a correct balance-sheet to the Registrar. The audit of the accounts of a registered society is compulsory once at least in every year. While audit is good and essential in the interest of members, the performance of the same function by the persons who are controlling the whole movement is nothing but a mockery of the whole show. The situation at present, in the words of the *Review* published by the Reserve Bank for the year 1930-40, is as follows: The systems of audit differ to a certain extent in different provinces. In Bombay, Sind, Bihar, Orissa, the United Provinces and Assam, the audit is conducted exclusively by the staff engaged by the Co-operative Department. Though some banks are audited by registered accountants as well, such audit is not recognised as a substitute for the Departmental audit. In Madras, Bengal, and the North-West Frontier Province, too, the audit is done by the staff of the Co-operative Department, but the Registrars permit audit of some institutions by registered accountants as a substitute for audit by the Department. In the C. P. and Berar, audit of large societies is done by circle auditors who are employees of the Co-operative Department, while audit of small societies is ordinarily done by society auditors working under the control of the Registrar and paid out of the Registrar's Audit Fund. Apparently the auditors are the creatures of the Registrars depending upon the latter's favour; and where audit is carried out by the departmental staff, the work is all the more smooth. In this respect, of course, the law, which requires that "The Registrar shall audit or cause to be audited by some person authorised by him," is defective; but the practice also has not been able to get rid from this defect.

Registration, however, offers certain privileges on the society. A registered society acquires a legal personality by the name under which it is registered, with perpetual succession and a common seal and with power to hold property, to enter into contracts, to institute and defend suits and other legal proceedings and to do all things necessary for the pur-

poses of its constitution. It enjoys a prior claim, subject to the claim of Government in respect of land-revenue or any money recoverable as land-revenue or of a landlord in respect of rent or any money recoverable as rent, upon the crops or other agricultural produce or any thing like cattle, fodder, implements and machinery, etc., supplied by it, over any other creditors. In certain other respects also, a registered society enjoys privilege, e.g., shares or interest of a member, in the capital of a registered society shall not be liable to attachment or sale, transfer of interest on the death of a member without any legal formality, exemption from compulsory registration of instruments relating to shares and debentures of a registered society, etc. In matters of taxation also it may enjoy certain privileges if granted by the Governor-General in Council.

As regards the property and funds of a registered society, there are certain prohibitions and safeguards. The law imposes certain restrictions on loans and borrowings from non-members, and other transactions with them, as also on the security offered against loans. The investment of funds by a registered society should be made in the Government Savings Bank or in any of the securities specified in Section 20 of the *Indian Trusts Act, 1882*, or in the shares or on the security of any other registered society, or with any bank or person carrying on the business of banking approved for this purpose by the Registrar or in any other mode permitted by the rules. This is not all. In order to safeguard the capital structure of co-operative concerns, special provision has been made in the law. Thus no part of the funds of a registered society shall be divided by way of bonus or dividend or otherwise among its members. As regards net profits, at least one-fourth of them in any year must be carried to a reserve fund but of the remainder or of any profits of past years available for distribution, payments may be made among the members to such extent and under such conditions as may be prescribed by the rules or bye-laws. In the case of societies with unlimited liability, no distribution of profits can be made without the general or special order of Local Government. The provisions are sound enough, but the provision regarding the investment of funds, though sound, seems rather in-

appropriate. If the object of co-operative movement is to supply cheap credit to members, the above-mentioned provision requiring the investment of funds in Government, semi-government or approved securities would frustrate the very purpose for which the movement was started. Only in so far as investment is permitted "in any other mode permitted by the rules", the members may come in as recipients. But even in this matter the working of the provisions of the law have not proved much successful. If a thing is to be judged by the results achieved, then it may be mentioned that "At the end of 1939-40 the societies had loans of Rs. 23.14 crores outstanding of which loans for Rs. 10.71 crores or nearly one-half were overdue. The real position would appear to be much worse in view of the common practice in several provinces of granting extensions and the unsatisfactory and varying systems of calculating overdues. Moreover, no accurate figures of overdue interest are available though its amount would appear to be considerable." A study of the working capital of the concern also reveals the weakness of co-operative movement in this country. It is peculiar, as is visible in the following table, that the weakness in working capital position is in **inverse relation to the intensity of official control**. Bengal having the maximum control but low average of working capital, while in Bombay where "probably the movement for deofficialisation has made the greatest progress," and "where the Registrar is reported more amenable to the suggestions of the Provincial Institute than in most parts of the country," the average-working-capital position per unit is the best.

Number of societies, total working capital and average working capital per unit of societies (including societies in liquidation) at the end of 1938-39:

(Figures 2 and 3 taken from *Review of the Co-operative Movement in India, 1939-40*, R. B. of India Publication.)

1	2	3	4
Provinces.	Number of societies.	Total working Capital. (Rs. lakhs.)	Average working capital per unit. (approximate.)
Assam	1,551	88	5,673
Bengal	30,707	2,021	6,581
Bihar	7,762	4,65	5,990
Bombay	5,126	1,627	31,740
C. P. & Berar	4,764	543	11,397
Madras	13,759	2,271	16,825
N.-W. F. P.	822	27	2,284
Orissa	2,704	132	4,881
Punjab	24,322	1,714	7,047
Sind	1,397	328	23,478
U. P.	10,858	321	2,956

Various provisions have been added to the acts to prevent capitalist interests from prevailing. In English law the shareholding of a member is limited to £200; and in the Indian Act it is limited to Rs. 1,000. In the language of Indian Law, where the liability of the members of a society is limited by shares, no member other than a registered society shall hold more than such portion of the share capital of the society, subject to a maximum of one-fifth, as may be prescribed by the rules; or have or claim any interest in the shares of the society exceeding one-thousand rupees. Unlike the shares of the joint stock company, the shares of co-operative society are not transferable to non-members, except in England. All co-operative societies make the value of their shares as small as possible to bring them within the reach of the poor, though there is no express provision to that effect in the Act. In the case of company shares also, a similar development may be seen with a view to popularise the shares among investors of limited means. But, although the shares of a co-operative society are not transferable, the members may withdraw their money by giving proper notice.

The relations between the members and the society are personal and non-capitalistic. In this matter, there is slight resemblance with partnership in so far as the relation between members is personal, though, of course, in the object of business, there is a lot of difference between the two. The societies are free through their committees to refuse admission to any individual they may deem improper without assigning any reason for that and in their bye-rules they place restrictions on the classes of persons who may join or the place from which members may be taken. There is a minimum number of members which must be there before a society begins functioning, in India, the number being 10.

The members of a co-operative society enjoy certain rights and have liabilities. Thus members are prohibited from exercising their rights till due payment is made, and membership acquired. Each member enjoys the right to vote. Thus where the liability of the members of a registered society is not limited by shares, each member shall, notwithstanding the amount of his interest in the capital, have one vote only as a member in the affairs of the society. Where the liability is however limited, each member shall have as many votes as may be prescribed by the by-laws. One of the most effective weapons of co-operative control on the continent of Europe is an obligation upon members, enforced by the imposition of a fine, to conduct all or a given percentage of their custom exclusively through the society for a given number of years. In England, also, in the model rules of British stores, there is a clause to the effect that any general meeting may fix an amount which every member shall be required to purchase from the store and if he fails to do so, he shall be returned his money and shall cease from membership. In South Africa the law lays down that if in any area 75 p.c. of the producers of an agricultural commodity are co-operatively organised and handle 75 p.c. of the product, the minister may, on the request of that co-operative organisation, prescribe that all producers within that area shall sell their product through the co-operative society. Besides, the law in most countries provide penalties for disobedience or negligence of certain precautionary measures. They are absent in the Indian law because it was felt that they are pre-mature. Provi-

sion for penalties is however made in a modified form in the *Bombay Act* of 1925.

In recent years it has been very much emphasized that the organisation of a co-operative society should be made all-comprehensive so as to include as many aspects of the members' economic life as possible within its scope. Upto this time, co-operation has remained a credit supplying agency and that, too, supplying only a microscopic proportion of the total need of agricultural finance. For a more successful development of the organisation, multi purpose societies have received support from many quarters in India and experimented upon in some foreign countries. While not decrying the need for a more comprehensive organisation, we must say that the picture envisaged by the Reserve Bank of India in this matter is too ambitious. The picture envisaged is as follows: "Starting with credit for current needs, a society may get the old debts of its good members liquidated through a land mortgage bank, introduce better business and better monetary return by inducing its members to sell their produce co-operatively, ensure their growing the improved varieties of crop by purchasing seeds for them, save on purchases by arranging for the purchase of their other needs jointly and at profitable rates on an indent system without incurring any risk or liability, save litigation expenses by effecting arbitration, improve the output of crop by consolidation of holdings, supply of pure seeds and improved implements, implement the income of its members by inducing them to take up subsidiary industries, introduce better living measures by adopting bye-laws by common consent which will curtail ceremonial expenditure and remove insanitary habits, provide medical relief and so on." A nice picture indeed. But the problems are threefold. In the first place, too much insistence on official control stands in the way of multi-purpose organisation; for, the villagers brought up in an atmosphere different from that prevailing in the officialdom would be the last persons to submit their lives to the fullest possible control. Secondly, the organisation scarcely contains right type of men imbued with co-operative spirit. This has often been misrepresented as the scarcity of proper men. For, the personnel of the co-operative organisation depends in the matters of selection and continuance on

the goodwill of the boss and therefore proper men who can really serve the country and have real interest of their countrymen at heart can scarcely come in. And finally, to expect good co-operative organisation with rotten agriculture and backward industry and commerce is to expect too much. The real experiment with co-operation as a form of business organisation can only follow, and not precede, the development of the economy of a country, for, as already indicated, co-operative organisation is a *via media*, between capitalism and socialism, intended to remedy the evils of existing structure without bringing its total collapse.

Supplementary Note:

The Congress Government in Madras has introduced a new scheme of co-operation whose aim "is to create a socio-economic fabric based on the co-operative principle in as high a degree as possible so as to enable the society to have its production and distribution of its essential needs planned and worked out in the interests of the people and thus eliminate or minimise the chances of private profiteering, hoarding, black-marketing and corruption." Some features of the scheme are as follows: A producers' co-operative society is to be formed for a contiguous group of villages for procuring the surplus grains available and distribute them among the villages in the area. If there is a surplus, it will be utilised for other areas, and deficit is to be covered by imports, not through wholesalers but through Government agency. Its membership is to consist of all producers and consumers who agree to take shares. The capital will be raised by the issue of shares of the value of Rs. 5/- and Rs. 25/- in Malabar and Rs. 25/- in the Circars Districts, an upper limit of Rs. 2,500/- worth of shares being fixed for any holder. The capital is to be fixed by taking into account the aggregate purchase value of foodgrains and would roughly be 1/10th of this value as the Central Co-operative Bank can advance upto ten times the basic capital of the society. (*Eastern Economist*, January, 24, 1947.)

PART II

ASPECTS OF ORGANISATION (Contd.)

CHAPTER VI

ORGANISATION OF HOME TRADE

The principal agencies in home trade of any country may broadly be classified into two—distributors of foreign goods and distributors of home-produced goods. These, in their turn, are sub-divided into different branches according to the nature and extent of the trade, the object in each case being the earning of maximum profit. It is the purpose of the present chapter to consider these organisations, as far as possible, under Indian conditions.

Distributors of foreign goods.

The justification for this type of trade arises from the justification of import trade. Goods are imported in a country for certain reasons. The traditional arguments of absolute and comparative cost advantages are too well-known to need recapitulation. Another type of import consists of raw materials from the colonies by the mother country for feeding up of the manufacturing industry at home. With the gradual development of political consciousness of the colonies and their industrial development, a large portion of these raw materials are consumed by the colonial manufacture and therefore a drive started towards the less developed regions and further scramble for colonies. In recent years the import trade is subjected to a variety of restrictions, either to preserve home market for own products or to accumulate foreign resources for the purpose of their better utilisation in the purchase of materials and necessary products which are not produced at home, or to develop an autarchic national economy thereby reducing its dependence on foreign countries in times of war. India's case is peculiar and falls under none of the above categories.

A study of the history of India's foreign trade shows that India had been a manufacturing country with "*Karkhanas*," even towards the close of the Mughal regime and Indian manufactured article was sent to the world market. Then came the

turmoil, the breaking up of empires and kingdoms, the onrush of Western power, and out of this, India emerged as an agricultural country—rather “reduced from the state of a manufacturing to that of an agricultural country.” But that is history and the verdict on the new administration in India has been given by the great historian, Wilson. But the fact remains that even to this day India has remained a country importing manufactures, a process which started with the rise of the Company’s Rule in India. The arguments of comparative and absolute costs are of no use, for, India having a great supply of materials for industrialism cannot but have absolute cost advantage over many other countries where most commodities are imported. The fact is that India imports not because she cannot produce nor because she has no advantage in production, but because of certain factors too well known. India’s is an economy where the home market cannot be adequately protected because that would inflict so-called suffering on consumers and even when protected, the tariff wall can be jumped over by any foreign concern which then becomes as good as a ‘national concern’ working against the national interest! India’s is an economy where there is no arrangement for the accumulation and proper utilisation of foreign resources, as is evidenced by their frustration during the first great war, their blocking during the last one, the conversion of dollar resources into sterling ones and the creation of Empire Dollar Pool, whatever the need and justification for imports for India, we consider below the organisation of the machinery in one or two cases, which will be sufficient for our present purpose.

Goods may be imported into India either by the agents of the foreign producers working in this country or by the selling organisation of some foreign producers direct or by the Indent Firms working for inland distributors. Let us take the case of imported piecegoods. The following description of the organisation is given by the *Bombay Provincial Banking Enquiry Committee*. It is to be noted that only a few merchants have direct connections with the manufacturers or shippers abroad. The majority of them buy through the importing firms. Some of these importing firms get accommodation from exchange banks, who on some occasions take deposit before accommoda-

tion is granted. The usual form of credit is the documentary credit which is an authorisation by the importer to a bank to make advances to the exporters on presentation to the bank of the bills of exchange and complete shipping documents. The shipping documents along with the bills go to the banks and they hold the goods until they are delivered to the consignee or his agent. The banks used to allow piecemeal delivery free but they have practically stopped the practice. If the consignee needs funds for taking delivery of goods, he is given a loan against the security of the goods up to 12 months or even for a longer period. Piecemeal clearance of goods is however allowed in cases in which the importing houses, finance the merchants. Goods are usually stored in port trust warehouse and delivery order is given by the importing firms.

When the goods are imported direct, they are generally handled on landing at the port by agents of the buyers. Where importing firms are intermediaries, they work through their agencies in Bombay and upcountry. The commodities then pass from the banks through whom credits are opened or from the importing houses to wholesale dealers in Bombay and other important centres of business; the wholesale merchants in turn sell the goods to local or mofussil retail merchants, the transaction taking place in most cases through the agency of a commission agent. The commission agent is responsible for the payment. Often a period of three days is allowed for payment; in some cases a week is allowed; after one week interest begins. From the mofussil merchant, the goods pass on to the village trader and thus reach the remotest corner of the country. The machinery of inland distribution of foreign goods thus differs from that of the internal trade, first, because in the former case, banks play a very important role which in case of inland trade is played mainly by indigenous bankers or commission agents working as financiers and second, bonded warehouses are utilised which are non-existence in internal trade.

In Calcutta also the distribution of foreign imported goods takes place exclusively through wholesale merchants of the port. These wholesale merchants are sometimes themselves importers but more often they buy from importing houses. The goods lie in their own godowns or in the godowns of the banks or of the Bengal Bonded Warehouses and sometimes

also in the Port Commissioners' warehouses. Some of the wholesale merchants of Calcutta have branch establishments in important mofussil centres where they send goods according to the requirements of the particular centre; but generally mofussil buyers come to Calcutta for making their purchases from wholesale merchants. After one or two transactions on cash basis, credit is allowed to these mofussil merchants, the extent of which depends on the financial position of the buyer, while the duration is different in different trades. The wholesale merchants naturally include in the price the interest for the period of credit. Smaller mofussil merchants generally prefer to trade with their own resources. So far as the Calcutta wholesale merchant is concerned, he relies mainly on his own resources and only when these prove inadequate, he will go in for borrowing. The mofussil merchant, in his turn, grants credit, whenever necessary, to retailer in his locality, whose transactions are also both on cash and credit basis. There is still another agency acting as intermediary, viz., the *aratdars*. These *aratdars* also supply their mofussil clients with imported goods as they want, on commission basis. Sometimes these *aratdars* act both as buying and selling agents for mofussil merchant, the latter's account being credited for the goods he consigns and debited for his purchases, the account being settled periodically, generally once a year.

Sometimes, under the pressure of circumstances, the importing merchants have formed an organisation of their own, combining all interested in the particular trade, the most notable example of this being the Bombay Native Piecegoods Merchants' Association. The formation of the Association is an interesting story. Piecegoods coming from Manchester used to be shipped by shippers, the Bombay merchants agreeing to pay a price based upon a certain rate of freight; but they enjoyed a rebate from the shipping company by using the ships of the Conference Line and did not share it with Indian importers. When the Indian importers came to know this, they became determined to secure the rebate for themselves and formed the above-named association for the purpose which immediately opened negotiations with outside steamship owners and placed their freight contract for the conveyance of Manchester indent goods at a much cheaper through rate. At

first it was felt by the Manchester shippers that the Association would not be able to continue its activity for long; but soon it was discovered that contrary to their expectations, the Association has grown up in strength and influence.

Distributors of Home-Produced Goods—Wholesale Trade.

The distribution of home-produced goods is undertaken by two types of agencies—wholesalers and retailers. It is often argued that the commodities reach their ultimate consumers through the retailers. This being so, the wholesale merchant is a superfluity, simply raising the price by his existence. On first hearing, the argument seems plausible. But a closer analysis is essential before one gives his verdict. For, the superfluity or otherwise is to be determined, not by stock arguments, but by the services rendered by the wholesaler in the trade. Since in India we are, under existing circumstances, concerned with agriculture, in the main, let us see what type of service is rendered by the wholesaler in this field. For, in addition to the general distributive activities which may as well be performed by the retailer, the wholesaler renders a lot of other services which make him essential in the particular trade to the extent to which these services are required.

In the field of agriculture, as also that of certain industries, assembling of products become essential from different sources before they are passed over to the ultimate consumer through the intermediary of the retailer. The retailer being a small man with small resources and information and having almost no specialisation is not in a position to undertake this function with economy. Of all the agencies for assembling the product, the wholesaler is by far the most important. Take the case of paddy. In this, we find the following agencies for assembling purposes: (a) cultivators, (b) growers who collect the produce of other cultivators, (c) landlords, (d) village mahajans, (e) itinerant merchants or *paikars*, (f) wholesaler, (g) rice-mills' agents, (h) professional dehuskers and (i) co-operative organisations. Of these, the share of the cultivators, according to some estimate, in the direct handling of the total marketable surplus, is less than 20 p.c., the first in the list being the wholesaler, to be followed by mills' agents. Some of these agencies,

again, *e.g.*, growers, village mahajans, and itinerant merchants or *paikars*, very often act as agents for wholesaler, working on commission basis, or on their own account, sometimes the latter giving advances of money to them. What is true of rice is also true of other products. The wholesaler also renders a lot of service in matters of standardisation and grading. Often the meaning of these two words is confused, which should, at first, be clarified. The service of sorting out products into uniform kind, quality and size is known as grading. Standardisation is the maintenance of the grades so arrived at over a period of time till the commodities are totally sold out, by removing those portions of the stock which have degenerated or deteriorated. The importance of these services in trade is quite well-known. They not only maintain the quality of the product but also lessen further waste and encourage forward business and long distance trading. In view of the fact that the produce of the individual agriculturist is small, and there is no special agency for grading and standardisation, the wholesaler acts not only as principal assembling agency, but almost sole grading and standardisation agency as well. This however should not be taken to mean a grading and standardisation on the countrywide basis. Whatever little is done in this respect in the producing area is done by wholesaler. In the matter of storage also, the assistance rendered by wholesaler is by no means negligible. The inadequacy, and, at the same time, the pressing need of storage in India is well-known. The cultivator has no adequate storing facilities nor can he always store in view of the pressing need of money immediately after harvesting season. Consequently, a greater part of the crop raised is marketed. If the wholesaler does not store it, there will be a glut in the market immediately after harvest and scarcity as the year rolls on. I do not overlook the defects of the present system when emphasizing its services; but in the absence of better facilities, the services rendered by wholesaler must be appraised. In matters of transport also, which requires specialised knowledge of different lines, the wholesaler is of some service. Since he despatches goods in bulk, he is in better bargaining position as to freight. In very big firms, there may be a special branch for the purpose of despatches. Naturally they can avail of the

best services at the cheapest rate by virtue of their special knowledge in different lines. The retailer, being a small purchaser and saler, cannot avail of these, unless, of course, his business is carried on on a very large scale. For all these and various other services, including the financial facilities they often grant, the wholesale link is essential.

The wholesale trade may be carried on on one's own account or on commission basis. When the wholesaler is acting on his own behalf, he is to handle the transaction from the purchase of goods to ultimate sale; not only that; he undertakes the responsibility for profit and loss and also of dead stock in case he makes a wrong purchase. An advantage of the commission business is to be found in the fact that the commission agent, unlike the trader on his own account, does not take the risks of trade himself. To some extent he resembles a salesman in so far as his interest lies in the furtherance of sale. The greater the volume of sale, the greater the total of commission that he earns. But whereas a salesman proper is a hired employee and, whether he advances the sale or not, he will be drawing his salary, the agent is a trader acting on commission basis, his interest lying in the pushing of sales, which, in its turn, will determine his remuneration. Sometimes, of course, the salesman is offered, not only the salary, but also commission, if he can increase the sale, the latter being a sort of further inducement. In this case, the salesman partly resembles the agent and partly the salesman proper. The agents generally specialise in a particular line, nor is it advisable for the producer to engage as agent one who is already employed in the service of some other producer. The mutual selection, of the agent by the producer and of the producer by the agent, is a bit difficult task. For, on the one hand, the manufacturer cannot afford to make mistake in his selection; otherwise, his products will not be sold in the market. On the other hand, the agent must be satisfied that the producer for whom he is going to work exclusively manufactures a product or products for which there is sufficient demand in the market and that he will be able to procure an uninterrupted flow of these goods according to the requirements of the market at a price lower than, or at most equal to, the price of similar products or its substitutes. Sometimes

it becomes essential to divide the agency, when the manufacturer manufactures different lines. But only in extreme circumstances should an agency be divided in the same geographical area. If it is possible for the same agent to handle the different lines of products in the same area on behalf of a single producer, he should be allowed to do so.

Sale on consignment is not the same in all cases but varies according to the responsibility shouldered and remuneration received. The literature on business organisation has so far discovered about a dozen variety. Of these, the principal types are universal, general and special agents. The universal agent has unrestricted authority to act for his principal in all matters. The general agent has general authority to act on behalf of the principal in all matters appertaining to a certain business. The authority of the special agent is however limited to a specific purpose only. Apart from these three principal types, we find so many other types of agents in commercial world, such as, commission agent, *del credere* agent, partner, mercantile agent, broker, forwarding agent, etc. In India, however, all these different types of agents are to be found. But, as in other fields, so also in this field, Indian agents have some peculiarity of their own, because of which a further classification would be more scientific. According to this classification, the agents may be divided into four classes: (a) buyers' agents, (b) sellers' agents, (c) specialised agents, and (d) non-specialised agents. Thus the indent firms, as already noted, act as buyers' agents. So also the *aratdars*. They maintain a network of communication with distant centres to which they supply goods according as they receive orders. In the same way, they act also as sellers' agents, receiving goods from producers, giving godown facilities to them, and sometimes even a certain percentage of the price of the commodity, and when the goods are sold, they realise not only their commission, but rent, interest and any other charges. The specialised agents generally deal in one or one major article, while the non-specialised agents deal in whatever article he gets. The distinction between these four varieties is however not clear cut, and there is, in most cases, a large degree of overlapping. Thus, e.g., the same agent may be working on behalf of the buyer and the seller. It may be argued, of

course, that for the sake of specialisation, these functions should be clearly separated; but in view of the fact that any particular line is not sufficiently profit-earning, this sort of overlapping is a matter of necessity.

But then no amount of classification of agents is adequate. I give below one instance in order to show what different types of conditions may come in in the agency contract. The illustration is taken from the trade in Indian piecegoods. This trade is carried on through a system of salesmanship known as the guarantee-broker system. The guarantee-broker deposits with a particular mill a fixed amount and he is guaranteed credit generally up to four times the amount of his deposit. He has to find a purchaser, or the mill finds one and the guarantee-broker guarantees payment to the mill by the wholesale merchant, though he does not purchase the goods himself. This is not a peculiarity of the piecegoods trade only; the actual contract between the principal and the agent varies from trade to trade and is determined by the peculiar circumstances governing it.

When the wholesale trade is carried on on one's own account, it may assume various forms. Thus the producer may himself combine the work of wholesaler. Where this is done, it is generally found that the work is distributed between two entirely separate departments. Where this is not done, there are agents between the producer and the wholesale merchant. The wholesale merchant may specialise entirely in wholesale business. Thus when one goes to some of the shops in the Canning Street in Calcutta, he finds that although the shops look like retail ones, yet their business is exclusively wholesale and they have nothing to do with retail. There are many merchants, again, who combine both retail and wholesale varieties. In this case, it is generally found that, apparently, the retail type is the main, and, at times, the retailer works as wholesaler and order supplier. He has another advantage in this respect. It is well-known that the business premises of a wholesaler may or may not be in the busy parts of the town; not so in the case of retailer. His premises must undoubtedly be in the most attractive quarters of the town or district of the town. Since he attracts all sorts of persons, he can find it advantageous to obtain

orders for his wholesale business. Even in western countries it is found that, in many cases, wholesale business has developed from purely retail types when the latter have desired to gain access to economies of buying. Where the wholesaler exclusively carries on wholesale trade, it may be of general type or of special type. When it is of general type, although there is specialisation in so far as it is wholesale, yet as regards the line of commodities handled, there is no specialisation. But in specialised type of wholesale trade, the wholesaler deals only in a particular line of wares. When there is a further specialisation, the wholesaler deals only in a particular type of commodity in a particular line. Thus, for instance, a specialised wholesaler may deal in textile goods only; but when further specialisation takes place, the wholesaler may be dealing in only, say, readymade cloth. All these types of wholesale trade are to be found in this country.

Organisation of wholesale trade.

In this country, two types of organisation are to be found in the whole trade—indigenous and foreign. In wholesale trade, foreign type of organisation is to be found restricted within a narrow scope. In this variety, the policy framing is done by the board of directors while the actual management is in the hands of the managing director. All the different departments are divided under two heads—administrative section and executive section. Administrative section is in charge of administration proper. Thus there is a secretary in charge of general administration and legal issues. In a smaller type of concern, even correspondence work, including the filing of old records and correspondences is also done under his direction. Where the concern is big, further division of labour necessitates the separation of correspondence work from general administration and while the latter is in charge of the secretary, the former is placed as a separate department with its own head. Accounts department also comes under administrative section. It is the function of this department to control cash, to maintain all financial records and to consider the question of credit sanctioning. In fact, this department plays a very important part. Since finance is the life-blood of

business, and since any future prosperity depends on the study of past records and future policy framed accordingly, the advice coming from the accounts department regarding the study of various costs and suggestions for their possible reduction are of invaluable importance to policy framers.

The executive section is concerned with business proper. So far as the local sales and deliveries are concerned, it is the function of the selling department to arrange them. They also receive orders from outside for the supply of goods and arrange accordingly. Another important function of this department is the purchase of goods. This necessitates a keen insight in market demand; for otherwise, the concern would suffer from deadstock. It must also keep itself abreast regarding the stock position, for, if the stock runs out, it will either have to purchase the same commodity from local market at a higher price to meet the requirements of the customer or it will have to regret his inability to supply immediately, which, in the case of new customer, creates an unfavourable impression. Therefore the study of stock position is vital. Where the delivery is to be given not locally but to a different place, goods are to be despatched and that requires a lot of work. For this purpose, the maintenance of a despatch department becomes essential. It is the function of a despatch department to check and pack the goods and do the work of invoicing and despatch. In this respect, also, specialisation has, on many occasions, saved a lot, particularly when the goods are to be transported from one political boundary to another. The separate department finds ample time to study the intricate formalities of despatch and because of their specialised knowledge can avail of the best transport and other services at cheapest cost.

This, in brief, is the organisation of wholesale trade. This division of work between different departments is the result of the growing complexity of business. The commercial invasion of the old world by the new, particularly in matters of business methods necessitated a change in methods and machinery of business and European countries are gradually adopting the American example in these matters. But so far as India is concerned, the impact of these is not as yet a violent one and she has still maintained her own typical

methods of organisation in most lines which are in the hands of the people of the soil. This organisation is less complicated and therefore less specialised. But, from the standpoint of efficiency, it is not possible to say that this or that organisation is comparatively better. It is all a question of the volume of trade handled. If the volume of trade is large, even the Indian concerns who have maintained their own organisation, would be found to make the organisation more elaborate. Thus there is one genetal manager looking into the management. There is a cashier as well. These two along with one man for outdoor work are the irreducible minimum. With the increase in the volume of work, the number of men is increased and a greater degree of specialisation introduced. But one thing is sure. In the Indian type of organisation of wholesale trade, scarcely a board of directors is to be found, the policy framing and general administration being looked after by the general manager, who always, or at least on vital matters, consults his master.

Purchase Policy in Wholesale Trade.

Needless to say, where the wholesaler is not himself the manufacturer, he obtains goods from the latter on his own account or on consignment and since his object is to make a profit out of this mere handling by creating a gap between the purchase price and selling price and since his object is to make this gap as wide as possible, without at the same time affecting adversely the market demand, but, if possible, increasing it, though not by rate cutting, but by better quality of commodity and better service, his object always is to purchase the best commodity in the cheapest market, and to avail the most convenient route for its transport to his place. This, in brief, is the underlying principle of the purchase policy. This must not be taken to mean that there is no stake in this trade. Although the wholesaler purchases in the cheapest market and tries to sell it in the dearest, his efforts may not always be successful and he may have to sell in a still cheaper market. This may be the result of a wrong purchase or misjudgement of market demand. He may withhold the supply for some time with an expectation that the market would revive; but

actually it may not. All these and a thousand other contingencies haunt him; yet a super-marginal trader would either be able to meet them or avoid them and make money. Sometimes there may be loss in one line but greater gain in another. On the whole he maintains himself, and, that too, successfully. The sub-marginal trader struggles for sometime and, if unsuccessful, has to yield.

At this point a slight diversion is called for. The concept of "total income" in economic theory even to this day has remained imperfect owing to the total neglect of wholesale trader in the determination of price. Let us consider the formulation of the concept of total income in Keynes' General Theory. According to him, the excess of the value of the resulting output over the sum of its factor cost and its user cost is the profit or the income of the entrepreneur, and the factor cost and the entrepreneur's profit make up between them the total income resulting from the employment given by the entrepreneur. This is only a partial statement. The total income from the employment should not only consider factors in production but also those in distribution where the process actually ends. For, the employment is given not for its own sake but for the sake of distribution. That being so, the true supply price will be determined by total cost of production plus total cost of distribution and that for a unit of output by total costs of production and distribution divided by the volume of output, and the total income resulting from the employment given by the entrepreneur is the aggregate of profits to the entrepreneur plus factor costs of production plus factor costs of distribution. True, the producer judges the situation of market demand from the order that he receives from the wholesaler and the greater the price at which he can sell to the wholesaler over the factor cost and user cost, the greater will be his proceeds over factor costs; but these proceeds in their turn depend on the nature of demand coming from wholesaler which in its turn is being shaped by the demand in the ultimate market. If, after adding the costs of distribution, the wholesaler finds that he cannot get a good market, his demand will naturally contract and this will have unfavourable repercussion on the surplus of proceeds over factor costs of the entrepreneur. Therefore, it is inadequate and

partial to say that the excess of proceeds over factor costs will determine employment; for the determination of the volume of employment must consider how these proceeds are being shaped and reshaped by the final market through the intermediary of the costs of distribution.

To come back to our discussion proper, purchases made by the wholesaler may be of various types. We have already seen how purchases are made, either direct or through indent firms, of goods manufactured abroad. Purchases may also be made from manufacturers at home. Most often these are made through some mill agents. We have seen how it operates actually in the trade in Indian piecegoods. These agents maintain their offices in principal trading centres; sometimes they appoint travelling agents in the interior with a view to collect and pool the orders and then place them with the manufacturer. This method is very much convenient to the manufacturer as well as to the wholesaler. Since the manufacturer has not to look after the trading side, he can devote wholeheartedly to production. But a factor of greater importance is that he can avoid to a great extent the credit risks, inherent in trade, by dealing with a few well-capitalised wholesalers. Purchases are also made from small producers. This is a very familiar feature of agricultural marketing in India. The smaller producers being scattered in the interior find it difficult to come to the wholesaler. So oftentimes the wholesaler appoints either itinerant merchants or *fariahs*, or obtains the services of independent small traders of the particular region in the collection of the produce. The itinerant merchants or *fariahs* are generally appointed on commission basis; but the independent trader does not receive any commission; he purchases from the producer at a price and tries to sell it at a higher price to the wholesaler the difference constituting the profit. Co-operative sale of agricultural products, direct, to the elimination of the middleman element, will be of great assistance to the producers. If the producers form their own organisation for this purpose they can eliminate the *fariahs* or small traders and bring their combined produce to the wholesale merchant. In this respect, however, the individualistic spirit of the agriculturist, and his unwillingness to have his products mixed with that of the same quality from

his neighbour, have stood in the way of co-operative sale by the agriculturists to the wholesaler in parts of the country.

Sales organisation and policy.

In the matter of sales organisation, the wholesale trade differs from retail trade. In the retail trade, goods are sold in very small quantities, sometimes only one unit of a commodity; the purchaser makes his selection out of a large number displayed before him. In wholesale trade, since the retailer is the customer, and since he knows, unless he is a beginner, the goods he requires, he simply places orders with wholesaler and obtains his goods. When the wholesaler comes to handle some new product he may offer inducement to the retailer so that the latter may strive to push its sale. He may give some concession in price or commission or in some other way. But when the trade takes place in an already known product, all the terms and conditions are pre-determined and the subsequent trade transactions are carried on accordingly.

For this purpose, the wholesaler maintains, as already seen, a sales and a despatch departments. The selection of personnel of these departments should be made with absolute care. In advanced commercial countries, provision has been made for a system of special training in this matter. It is the function of salesmen not only to push the sale but also to study the trend in market demand and adjust the supply to the changing requirements. Many firms of wholesalers appoint travelling agents whose function it is to obtain orders from standing customers, to convert the prospective customers into regular ones and to revive the dead accounts. Salesmanship is a great art in the field of business and therefore much depends on the personality of the salesman and his influence.

Sales policy is nothing but a selected and continued line of action in the field of furtherance of sale carried over a period of time. Sales policy is a comprehensive term and includes so many things in its scope. In the first place, the trader must obtain information regarding the demand for his goods. Various devices may be adopted for this purpose. Of these the most familiar in this country is postal communication with the retailers. But a more effective method not only of obtain-

ing information about the existing demand but also for pushing the sale among prospective retailers, occasional personal visit is more effective. When the information has been received and orders obtained, it is necessary, for a successful sales policy, to see that the orders are properly handled and goods selected, packed, checked and despatched to the utmost satisfaction of the buyer. Although we have said that sales policy should be a continued line of action over a period of time, yet rigidity in these matters is the fruitful cause of failure in many a lines. So it must be as flexible as the circumstances permit, changed and adapted to the requirements of the situation. A more effective sales policy is backed by market research. At first sight the money spent for market research may seem to be a wastage; but actually it is paying, if not by developing sales, at least by saving expenses and preventing disappointments accompanying an attempt to enter a market which is already over-congested or where no demand for a particular product is at all possible. Where concerns are small, a combined market research may be instituted. It is in this respect that the Indian trade seems to have given the least attention. The method of research carried on by many wholesalers is rather crude and is only a part of gathering of information by postal communication, and sometimes by hearsay which afterwards is followed by a formal introduction by postal means.

The methods of wholesale sale, and price quotations therein, of agricultural commodities in India are an interesting study. When goods are sold in fairs, three methods of sale are prevalent, *viz.*, sales under cover where the price is fixed by the pressing of fingers under the cover of a piece of cloth, auction system where the deal is closed in favour of the highest bidder and open bid or private treaty. In the last method, rates are settled openly, but there is no shouting as in the case of auction. The goods are displayed and price is fixed, according to their quality and according to the intensity of market demand, by any of the above three methods. In more organised wholesale trades, *e.g.*, that in rice or wheat, etc., sales on sample are more prevalent. In this case, the value is assessed by visual examination only. Sales on sample prevail owing to a lack of uniform system of grading. This being the

case, sale by sample is often a cause of dispute, when inferior quality of goods are despatched. In the wheat trade of Punjab, sales on fair average quality and sales on standard contract are also prevalent. In the former type, the *Kachha Arhathiya* averages out the various lots that he receives from the local market and thus prepares a quality as a result of this mixture which is known as the "fair average quality" and then he undertakes group sales of varying quality at a flat rate. Thus his practice is to reduce all the different varieties into one common f. a. q. standard, so far as sampling is concerned. Sales on standard contract with the mills are also prevalent in the Punjab. The terms of the contract cover a description of deliverable wheat, quantity, price and source of its origin, and also of the type of bagging and terms of delivery, refraction and payment. The weights and analysis as ascertained by the mills are usually taken as final. The contract also contains various clauses covering non-delivery or failure to deliver. The options lying with the buyer are usually,

- (a) to cancel the contract in so far as it is unfulfilled;
- (b) to re-purchase at the market in which the mill is located, or elsewhere, at current market rates, such quantity as was undelivered, the sellers being responsible for any loss sustained by the buyers;
- (c) to charge the seller with the difference between current rate and the price at which contract was made; or
- (d) to grant an extension for the completion of the contract.

Where sales are made to comparatively distant markets, as is done in case of rice, either within the country or possibly to Ceylon and Mauritius, samples are not always sent in connection with each transaction, particularly in case of reputed varieties handled by well-known firms, many of whom may have their own selling agents in different selling centres. In such instances, a few samples may be exchanged, early in the season, to give prospective clients some idea of the quality of the current year's crop. Subsequently, business may be done on the basis of trade descriptions only. Occasionally large buyers maintain their own agents in important producing centres or their representatives may pay periodical visits to the

supplying markets to inspect the quality of the produce and make direct purchases.

It is gratifying to note that in some parts of India regulated markets have been established as a result of which efforts are being made to enforce suitable quality standards and standard contract terms. If these are enforced in all lines, a definite improvement in sales organisation would take place.

Price Determination and Policy.

A successful sales policy, in its turn, depends on a successful price policy; for, mere sale of goods is not enough for the trader's purpose; sale must be effected at a reasonable profit. This depends on the price at which a commodity is to be sold and price is determined by various sorts of costs involved in production and distribution. A study of various factors in cost is necessary not only for the determination of price but also for effecting economy, when called for, in the days of depression, thereby adjusting cost to price obtainable and maintaining its existence in bad days. The whole idea behind cost study and accordingly to introduce reorganisation have assumed special importance since the last depression, not only in other countries, but India as well. This is of special importance in case of agriculture, which is most effected by the depression. If the fixation of agricultural prices and their maintenance in days good or bad are not possible, there must be some method of price adjustment. The same is true in industries. But this requires a close and separate study of each item of cost so that those in charge with this particular aspect in trade and production may try to effect economy so far as practicable.

As in many other fields, so also in the field of price determination, the solution given by the economic theory is of little use. Elsewhere, we have seen, economic theory tries to find out the factors, not of price determination, but of price fluctuation. Most theories of prices in economics make two mistakes. In the first place, they consider "the way in which changes in the quantity of money affect prices," and secondly, by price they mean either the price of totality of output including services as in Fisherine

Analysis of the price of consumers' goods and that of total output as in Keynesian Treatise analysis. For an individual businessman these are vague concepts. He is concerned with the cost that he incurs in production and distribution and his object is fulfilled when he earns a profit on the sale of his produce. Here a question may be raised. If after producing an article, he finds that it is not earning enough to cover its cost, what will he do then? In this case it must be said that before entering in a particular trade, one considers its potentialities and if in first chance he is not successful, he will strive to effect economies and make his project a success. If he fails, he must withdraw after sometime.

But if that is so, what determines the price for him? Surely it is not the action and inter-action of the forces of demand and supply. In some cases, there may be no existing demand, *e.g.*, tea in its earlier stages. In such a case, there can be no question of action and inter-action, but demand is the result of creation. In others, it may be found that the market is already there and it is already supplied, at a certain price. If one is to enter into this field, he has to take the price for granted and explore possibilities for adjusting his costs to this price level in such a way that after meeting all of them, there remains a fair margin of profit. This is true of many Indian industries which find the Indian market already captured by foreigners. What determines the price in this case for the new comer? Surely not the higgling and bargaining between purchasers and suppliers, but the already existing prices, and under some circumstances, the possibility of price cutting, a fact with which we are quite familiar in many industries which had to face competition from foreign products.

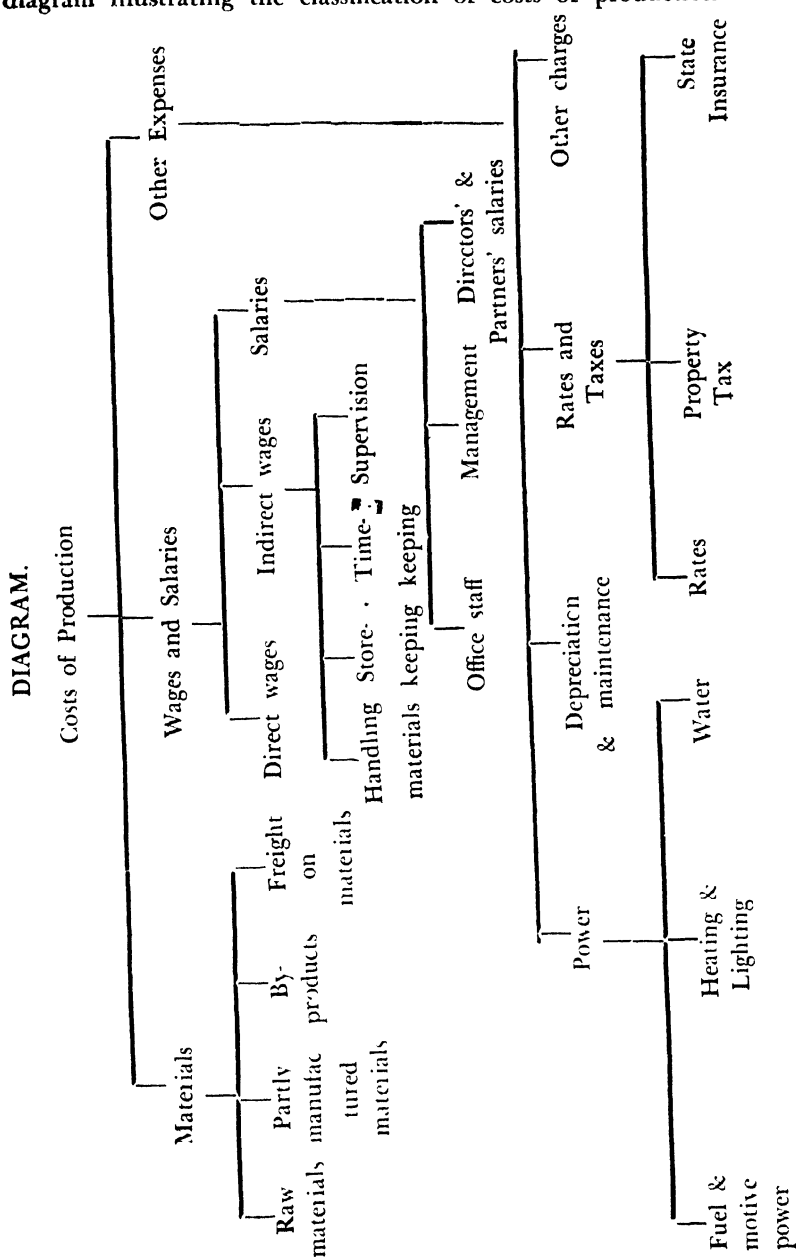
Prices may at times be raised and lowered by artificial measures. The volume of money may remain the same and so also the volume of commodities; the costs of production also do not change over a very short period; yet those who are familiar with the operations of produce exchanges, both Indian and international, know it quite well how prices of goods are fluctuating so many times every day; and although these fluctuations are normally small, the gap between the highest and lowest price quotations being narrow, in abnormal

times, although monetary, demand, and cost factors remain the same, yet as a result of the change in expectation, prices fluctuate to any extent. Thus expectation about the future not only determines the supply, but also the price at which commodities may be purchased and sold at a particular moment. It is not our purpose here to develop a theory of prices; we simply note some of the factors affecting price which are of importance from the standpoint of practical business men. One thing is, however, clear. In a dynamic world governed by continuous price fluctuations, any theoretical attempt at discovering the equilibrium point is futile; for in actual world, there is no equilibrium. Economics has left out the analysis of demand and satisfaction to psychologist and of supply and cost to cost-accountant. The demand and supply with which it deals belong to a world of its own.

Whether a business man will enter into a particular line or not, and if already entered, whether he will continue there or not, will depend on whether he can cover the cost in the price that he gets. The difference between total cost and total supply price obtained will not be the same. It differs according to various factors, *e.g.*, raw materials, labour, capital supply, management, size of the firm, etc., and according as the efficiency of these factors is greater in one firm than in another, the former will earn a higher profit. In the long run, only those firms can continue in business who are earning some profit, more or less, or who are not making any losses. As the *Balfour Committee* put it, "Producers differ in ability and opportunity; some have better equipped and situated works; some have better relations with labour; some have more successful advertising and selling organisation; some are in this country with similar conditions as to standards of living, while competing producers in other countries may be working under lower conditions. The competition of the efficient producer makes the trend of price towards the more efficient cost plus a profit. The less efficient makes a smaller profit, no profit or a loss."

The sum and substance of our discussion on price determination is that so far as the producer or distributor is concerned, he is interested only in one thing, *viz.*, costs, in whose calculation he cannot afford to make any mistake. The Com-

mittee on Industry and Trade in England adopted the following diagram illustrating the classification of costs of production.



The above diagram gives some idea as to how price is determined by cost factors. But so far as the ultimate consumer is concerned, a few more items for the cost of distribution, e.g., commission, storage, transport charges, insurance, labour of loading and unloading, cartage, etc. are to be added. Where goods are taken on one's own account, commission does not figure as cost. But other factors must be there and the trader will add his own profit at a certain rate. A specimen of the factors in distribution in some agricultural products is given below:

(1) Prime cost (of the article which has been purchased from the producer.)

(2) Commission (If on one's own account, profit at a certain rate.)

(3) Brokerage (When one purchases on his own account, the broker brings the producer and the purchaser together.)

(4) Postage (Actual or fixed charges.)

(5) Labour (Filling and sewing.)

(6) Cartage (For sending to Railway station.)

(7) Miscellaneous charges at Railway station.

(8) Railway Freight.

(9) Tax, if any.

(10) Cartage from destination station to shop.

(11) Labour (For unloading.)

(12) -Bardana.

(13) Godown rent (When on consignment.)

(14) Insurance.

Whatever may be the costs of production and distribution, actual price depends on the price policy pursued by the concern. This actual price may be equal to the costs of production and distribution, may be in excess or may be less than that. It all depends on the policy pursued. The policy in its turn is determined by various other factors, depending on the nature and usefulness of the commodity, the elasticity of demand for it, monopolistic or otherwise position of the seller, etc. Price increase by monopoly in case of those commodities which have an inelastic demand for them is not rare. If however it is found that as a result of price increase, demand is being adversely affected, having its repercussion on the excess

of proceeds over costs, any increase in price is not wise. But even this general statement should not be taken as fully correct. It is often found that even in competitive lines, a marked increase in price is being effected on the ground of superior quality, without at the same time adversely affecting the demand, although a better knowledge about the quality would show that the assertion is more a matter of propaganda than one of reality. The consumer is not a specialist, although he actually uses it. When he finds that it slightly differs from the other in shape or colour, he is at once duped. Changes in fashion every now and then is the most familiar example. Although the manufacture of a new variety of shirt does not involve any additional expense, yet the businessman knows that once he can popularise its use, he can earn a lot by exploiting the psychological weakness of the wearer. The psychologist may find out justification on the ground that the wearer gets a greater satisfaction and is therefore fully justified in paying higher price. But as practical businessmen we consider what cost does it involve and what price does it fetch, no matter for what weakness of the consumer. In some cases, price cutting is resorted to, particularly when a rival makes appearance or when a new market is to be captured. For the latter purpose different prices may be maintained in different markets, the loss in one being compensated by gain in another at the same time or greater gain in the same market at a later date when demand is stabilised or rival ousted. But where competition between different firms is equal, price cutting should not be resorted to; for, that would induce price reduction by all, to the advantage of none. But even then it should not be presumed that in a "world of monopolies" and imperfections, this is a shelter for classical economics. For even here, although in apparent price policy there is the trace of perfect competition, actually it will be found that ninety-nine out of hundred concerns offer concessions in some form or other that the price paid is not the same as that apparent but much less, some portion of the payment being received in payment back in money or service or kind. The case of deferred rebate system is too well-known. These are only some well-known cases. The conclusion that emerges is that, whatever the cost, actual price is charged according to the price policy of the

seller, which in most cases tries to obtain higher price, though in certain cases, lowering of price too is not unknown.

Credit worthiness and Credit Policy

The underlying feature of twentieth-century commerce is credit, and credit implies two things, *viz.*, incompleteness of the transaction and confidence in the solvency of the customer. This had on the one hand reduced the necessity of a large volume of money in trade purposes and on the other hand has increased the number and pace of business transactions. It is of course true that credit sanctioning in its turn has led to certain disadvantages, such as the locking up a part of the seller's capital, trouble and expense of maintaining a separate account of credit transactions, collection of payment from them, risk of bad debt, etc. But, notwithstanding these disadvantages, there is no denying of the fact that but for this device the development of trade would not have reached the same extent as it has done to-day.

It should however be noted that there is need for great caution in the sanctioning of credit. For, while a reckless sanctioning of credit, though leading to temporary expansion of trade, is, from the long run point of view, disastrous in so far as it leads to bad debt, too much cautious a policy is equally bad because it fails to attract custom and may therefore ultimately oust the firm from business. Hence the need of movement in step with others, except, of course, with those who are sanctioning credit, may be through inexperience, recklessly. It very often so happens that in these matters each trade has its own precise customs, which is observed by the old members and should be by the new entrants.

Leaving aside the question of credit sanctioning, there is another aspect of credit policy, *viz.*, credit control. Credit control may be qualitative or quantitative. Qualitative control applies as regards the period for which credit is sanctioned and any other privileges granted, and is governed mainly by trade usages, though, to some extent, by the financial resources of the firm. Quantitative control appertains to the value of goods supplied on credit, which depends, on the one hand, on the financial position of the firm and, on the other, on the

credit worthiness of the customer, as revealed in the enquiry from the references given by the customer, in banker's opinion, or by the facts and figures supplied by the commercial enquiry agents and publications, both official and non-official. Credit sanctioning is a matter of actual practice and varies between trades and hence nothing further can be added in this respect.

In big firms, where specialisation is introduced to the fullest extent, a credit department is maintained for enquiries in the credit worthiness of prospective customer. The functions of the credit department does not end with mere enquiries but also include the initial sanctioning or refusal of credit to particular buyers, and determination of its amount, keeping a close and continuous watch over the entire credit transactions of the firm, and paying attention to the matters of collecting debts from persons to whom credit has been allowed. But the maintenance of a separate credit department is not possible in case of small firms, nor are the agencies, particularly the commercial enquiry agents and publications, well-developed. Therefore the practice in this country is for the smaller firms to obtain information from the references given or from the persons or firms well-known to the selling concern in the place of prospective buyer, and to some extent from the banker. Postal means therefore play the most important part in credit enquiries in this country.

Conclusion—Trends in Wholesale Trade

The trend in Indian wholesale trade is towards the gradual elimination of the wholesaler. The process is very slow and therefore often does not attract the notice of a casual observer. The most outstanding instance in this respect is to be found in case of sugar and cement. With the formation of merger in various cement companies, the marketing function is now undertaken by the central organisation through its agents in different parts of the country. The same is also true to a great extent in the case of sugar. In many cases the same merchants who used to carry on wholesale trade on their own account become commission agents for the central organisation, when any such organisation is formed. In other industries, of course, sell on consignment is not a rare factor and

will increase in intensity as the pressure of circumstances lead to the formation of central marketing organisation for each industry or any considerable part thereof.

In agriculture, Punjab presents the most outstanding example in the experiment towards the elimination of whole-sale and also retail merchants through the instrumentality of co-operative commission shops. The members of these commission shops consist of individuals or co-operative societies. Membership may be compulsorily terminated if a member fails to sell his produce through the society for two years. According to the rules of business, all transactions by commission shops are on cash terms, subject to the practice of the local market which allows two days grace for payment from the date of weighing. No credit is allowed, except to a Government servant purchasing on behalf of Government. The sale is effected ordinarily by private agreement and, if desired by owner, in public auction. These shops therefore strive to breakdown the system of credit on the one hand and to deal directly with the exporters, on the other, to the total elimination of middlemen. In response to the demand created by large exportable surplus, a number of market towns have sprung up where world prices are daily received and transactions performed accordingly. The benefit derived by the members and the progress made by co-operative commission shops are illustrated in the following two tables:

(Source: Year Book & Directory of Indian
Co-operation 1942)

TABLE I.

Table showing the List of charges per Rs. 100/- for ready sales of all kinds of grain produce made by commission shops and other shops and difference between them:

		Co-operative shops			Other shops			Difference		
		Rs.			Rs.			Rs.		
Commission	...	0	12	0						
Weighment	...	0	3	9						
	...	0	15	9	1	9	0	0	9	3
Unloading of carts	...	0	1	0	0	1	0			...
Cleaning	...	0	1	6	0	1	6			...
<i>Dharmau</i> (a charge in cash for religious purposes)	...				0	1	6	0	1	6
<i>Ganesh</i> (a charge for giving alms)	...				0	1	0	0	1	0
<i>Gowshala</i> (a charge for refuge home for cattle)	...	0	0	3	0	0	3			...
Charity	...	0	0	3	0	0	3			...
<i>Chungi</i> (payment in kind to labourers)	...	0	8	0	1	0	0	0	8	0
Total	...	1	10	9	2	14	6	1	3	9

TABLE II. Progress of Commission Shops.

Year	Number of shops.	Produce sold in mds.	Produce sold (value in lakhs of rupees).
1930	24	1007284	41
1931	25	1214221	30
1932	25	894995	24
1933	23	545625	18.61
1934	22	695497	18.96
1935	22	700833	22.50
1936	21	709694	26.11
1937	21	576632	23.49
1938	20	650409	19.05
1939	20	825630	26.65
1940	20	817955	33.59

It will be seen that the new experiment has not been very much successful and has remained more or less stagnant. Although from table I it is clear that the benefits are real, it seems strange that the movement should not make progress. The reasons are many and need careful investigation. The disloyalty of the members is undoubtedly a factor; but if he realises real benefit, one fails to understand why he should prove to be so. To some extent the hold of existing agencies is responsible in this matter and to remove them, the co-operative commission shops should offer sufficient attraction. The shops are themselves not devoid of defects. Thus frequent embezzlements in some of the shops, discontent for not declaring dividends and granting rebates and the policy of the shops to invest large sums in sites and buildings for godowns, etc., have proved serious handicaps. The removal of these defects and the organisation of a central body co-ordinating and standardising their functions and usages and establishing greater contact with outside, both national and international, markets would be of great benefit for the shops and there is no doubt that if the shops make progress on these lines, they will be popular with agriculturists and will no longer be limited in the Punjab but find their way in the marketing of other agriculture products of other provinces as well.

This tendency towards the elimination of wholesaler is not peculiar to India but is equally true in some other countries, like England, where the tendency was markedly revealed in several evidences given before the *Committee on Restraint of Trade*. One of the recognised functions of the wholesaler is the purchase of goods in cheap market and their sale in the dear market thereby making equitable distribution of goods on the one hand and steadying the price level on the other, over a period of time. The scope of this activity on the part of the wholesaler has been restricted owing to the deals in fixed price or branded goods, and in these transactions the wholesaler has become an "absolute figure." Thus the *Committee on Restraint of Trade* in England writes that in such trades, the wholesaler has got "no opportunities of performing what are sometimes regarded as the distinctive functions of a merchant, that is to say of buying supplies in a cheap market and selling them in a dear market."

CHAPTER VII

ORGANISATION OF HOME TRADE

Retail Trade—its importance and recent tendencies

The retailer is the last link in the distributive chain and in the field of trade and commerce, his importance arises from the intimate contact that he has with the ultimate consumer. The object of the whole process of production and distribution is the sale of goods to the ultimate consumer; all intervening sales are mere transfers with a view to push the commodity in desired channel. It need not be said that in India the retailer occupies a position of great importance. Even in countries like England, America and Canada where the tendency is towards retail trade on a large scale, the small man is not totally ousted, but still holds his own in view of the peculiar position that he enjoys by virtue of his closer contact with his customers and ability to study their particular requirements. According to a rough estimate made by Lawrence E. Neal, himself associated closely with the retail trade in England, 45 per cent. or more of the trade of that country is in the hands of retailers. Although the turnover of these shops is small, yet he continues and signs are not lacking in these advanced countries that the force of competition from multiple organisations and departmental stores is compelling the small retailer to put his own house in order and to do a more efficient job. He is not only learning some of the techniques which the multiple shops have taught him and, in some countries, is beginning to form voluntary associations for the purpose of securing the advantages of bulk purchase. In matters of sale also, the retailer is modernising the shop fronts and improving his selling service. In this country, however, the impact of large scale retail trade on the small one is limited and more or less non-competitive. For, as will be seen, a few departmental stores, Indian and non-Indian cater for the needs of a few big cities and there too of a limited section of the population who pass for aristocrats or strive to be so. For, the prices in Indian stores are very

often higher than those prevailing in ordinary shops and the prices in departmental stores owned by non-Indians are so exorbitant that they attract very few ordinary customers. Therefore so far as the ordinary retailer is concerned, he is not affected by the competition from these big concerns, nor is there any reason to expect his being affected in the near future.

Forms of Retail Trade and their Organisation—Itinerant Trade

Broadly, the retail trade may be divided into two types, according as the transaction is carried on in a fixed locality or not. When the locality is not fixed, it is known as itinerant trade. But when transactions are carried on in a particular locality, it is known as local or fixed trade. Itinerant trade is a form of retail trade in which the seller has no fixed locality but carries his goods from one place to another. In fact, this form of trade is very old, but in civilised communities, it is losing its significance and will probably be restricted all the more in the future with the expansion of fixed shops.

The commonest type of retail trade carried on by the itinerant trader is that of the hawker and the pedlar. In this country we scarcely draw any distinction between the two; but in England a legal distinction is made. Thus the Pedlar's Act of 1871 defines a Pedlar as "any hawker, pedlar, petty chapman, tinker, caster of metals, mender of chairs, or other persons who, without any horse or other beast bearing or drawing burden, travels and trades on foot and goes from town to town or to other men's houses, carrying to sell or exposing for sale any goods, wares or merchandise.....or selling or offering for sale his skill in handicraft." The Hawkers Act of 1888 defines a hawker as "any one who travels with a horse or other beast of burden, selling his goods." With certain exceptions, a hawker in England must take an excise license. In America hawker was a more common figure carrying goods from one village to another. In this country, the pedlar is more common—a very familiar figure in the villages, and also in towns, sometimes carrying goods on a wheeled carriage. The use of animals is not very common. Whatever

that may be, the organisation of this trade is very simple. The pedlar may purchase goods on his own account either from a local supplier, or from wholesale dealer and, occasionally obtain them from his domestic production. He may also be working on account of somebody else in which case either he receives wages, daily, weekly, fortnightly or monthly, or a share in profits, and on very few occasions, both.

Another type of itinerant trade is that carried on by the street trader. Unlike the hawker and the pedlar, he does not shout and exposes his wares in a well frequented part of the town with a view to attract his customers. The hawker is mainly concerned with children to whom he can sell attractive or delicious things. But the street trader attracts grown up men, particularly the poorer sections. He does not remain in the same place but moves according to the change in traffic, say, from the railway station after the time of train departure to some other place where he can attract better custom. Sometimes he deals in secondhand goods or goods derived from auction sale or bankruptcy stocks, and then he may be known as Cheap Jack. In England these cheap jacks hire in a certain locality a shop in as good a position as possible, make a good display of the goods, employ all sorts of propaganda and sell as much of his stock as he possibly can. In India goods derived from auction sales or bankruptcy stocks are in most cases not so many as to induce the cheap jack to hire a shop. In Calcutta the most familiar type of street trading in secondhand goods is that in old books in which many people are employed.

Another type of itinerant trade is that carried on by the market trader. This however differs from the other itinerant trades mentioned so far because in this case the locality of trade is fixed in a particular place in the village or the town and it is at this spot that both buyers and sellers must assemble. It is itinerant because under the shed so allotted any one—purchaser and seller—can come from any place and carry on transactions. In India we find so many types of these markets. In the first place, there are the fairs, held occasionally, mainly associated with some religious festivals, some of them being very much extensive, attracting pur-

chasers and sellers from many parts of India. They have acquired considerable importance in the livestock trade and in trade in agricultural products. Now, their commercial aspect has assumed greater importance over the religious association. According to the *Report on Fairs, Markets and Produce Exchanges in India*, there are over 1700 livestock and produce fairs in India, the figure indicating the number of places where fairs are held. Out of these, about 50 per cent. of the fairs deal in livestock only, about 10 per cent. both in livestock and agricultural produce, while the remaining 40 per cent. handle agricultural produce only. Secondly, there are markets, known by different names in different parts of India, which also come under the category of itinerant trade. In this case the gathering of people takes place at a fixed locality and is more frequent than in the case of fairs, but the gatherings are not so large as in the case of fairs, for, unlike the fairs, the markets attract people only from a narrow area. They may be weekly, bi-weekly or may take place for more than two days in a week. Sometimes they may be held on all the days in a week, including Sunday, but the gathering taking place in a particular locality on a particular day, thus covering the whole of a big town in seven days. Thus in Poona, I found localities named as Rabiwar peth, Budhwar peth, Saniwar peth, and so on and in some other places in the Deccan, actual markets known as, say, Mangalwari Bazar. In Poona, however, these names of different localities have only historical significance from the standpoint of itinerant trade, in so far as the shops are fixed and open on all days in all these peths, although they retain their names even to this day. In these markets purchases and sales are of a retail nature. A wide variety of articles is available for sale. The producers, coming from neighbouring place, bring their small produces and dispose them of in these periodical markets. The transactions are on cash terms, although in certain backward tracts of Chhota Nagpur (Bihar), in dealings in *hats*, "the barter system also prevails. It was noticed at one of the *hats* held in Chhota Nagpur tract, that mustard was being exchanged for rice volume for volume, although the price of mustard in the nearest wholesale market—about 30 miles—was about 50 per cent. higher than that of rice."

The days for the assembling of different markets are fixed in such a way as to avoid overlapping with one another. Thus it is often found that the same persons are working as buyers and sellers in different markets on different days within a certain radius. The area served by these markets is not the same. In Bengal they are comparatively smaller, serving generally an area within a radius of about 2 to 3 miles, and at most 5 miles, whereas in Bombay they serve an area of a radius of 60 to 70 miles and in Madras 70 to 100 miles in some directions.

*Forms of Retail Trade and their Organisation—
Fixed Trade*

In fixed trade, the lowest stratum is occupied by the street stall holder. In some corner of a street, there may be a wooden stall, rented on auction for a period of time. These stalls generally deal in fruits, betels and betelnuts, bidis and cigarettes, and various types of cold drinks, etc. In some railway stations there are similar stalls selling books of current interest. The fixed stall holder represents a link, so to say, between the itinerant and truly fixed types. For, he is not itinerant in so far as he does not move from place to place nor does he shout. But then he does not belong to a truly fixed type, because he, being the highest bidder, has obtained the use of the stall for a certain period, but cannot be sure of permanent occupation in so far as on the expiry of the period somebody else may be the highest bidder and occupy it. The street stall holder obtains his supplies either from small local suppliers or wholesale dealers or from domestic production.

The truly retail shop is however the small shop selling articles retail. It may either be a general store or a speciality store. Specialisation is however out of question in those places where the market is narrow. Therefore at most all stores in small towns and most of them even in big towns are general stores dealing in a variety of goods, and distributing them among all sorts of persons. Speciality shops may be of different types—specialisation in one complete line, e.g., groceries, hardwares, books, clothings, etc., specialisation in allied lines.

e.g., photographic and painting materials, chemists and opticians, etc. and specialisation in a particular type in a particular line, *e.g.*, readymade shirts only. The degree of specialisation is not the same but depends on two factors—*viz.*, extent of demand and extent of market. For, after all, the trader is concerned with profits, and if the conditions of demand and of the market are such as to enable him to earn sufficient profits by the handling of one line or one variety in a line, he will not go in to handle thousand lines at a time. But where any one of these conditions only is satisfied, specialisation becomes difficult; and in the absence of both, specialisation is impossible.

Before starting a retail shop, whether general or speciality the proprietor should estimate the financial requirements and the equitable distribution of his funds on different requirements. For, in most cases, he is a man of small resources which are supplemented by deposits or loans from friends and relatives. Therefore any injudicious investment would not only put him out of his own funds but also lead to a waste of these loans and deposits. So, before entering into business, it would be advisable for the proprietor to estimate the different financial requirements. The financial plan will no doubt depend on the nature and extent of the business that he is going to undertake and also his own credit in the market, which will determine the extent to which he can dispense with money in his initial purchases. The maintenance of stock also requires money, but the demand on this score will vary according as whether the store is a general one or a speciality store. In the latter case, because of specialisation, the money blocked in stock is comparatively small, for, in general store, he will have to maintain some stock of each line and therefore require a greater amount. In case of special store, the proprietor comes to enjoy another advantage. Since he is dealing with one or very limited number of wholesalers, as compared with that in general store, he attains a greater degree of intimacy and therefore there is a greater possibility of his obtaining more and more goods on credit. Then there are certain items of expenditure, which are, if we may say so, supplementary costs to business, in the sense that whether the proprietor makes any profit or not, he will have

to meet them. In this category falls items like rent, wages, lighting, etc. As long as he continues in business, he must meet them irrespective of whether returns accrue to the business or not. Besides, there are so many possibilities of troubles in the initial stages of business and unforeseen contingencies even when business has made sufficient progress. The proprietor must be prepared with funds to meet these "strides" and contingencies, which are, so to speak, a test of his business acumen.

The organisation in retail trade is a bit complicated in so far as it involves not only the organisation of business but also the organisation of the shop. It is in this respect that it differs from wholesale trade. In wholesale trade, the trader is to maintain his office and an organisation of business which is sufficient for his trade. There is no need for his selecting a suitable site. His warehouse may be in any part of the town, the main criterion being nearness to the transport facilities. Not so in case of retail trade. Since he is to deal with ultimate consumer, the organisation of the shop is more important than even the organisation of business.

The organisation of business in retail trade has to consider three things. In the first, and most important, place, comes the shop, for which there is the need for the judicious selection of site. In this respect the general rule that can be laid down is that the busiest place is the most suitable. At first it may sound strange that the busiest place where there are so many shops already doing business, is instead of being the least suitable, most suitable. Any one inexperienced in business will say that since a shop in, say, Esplanade in Calcutta, would necessitate the payment of high rent, how can it be most suitable? On the contrary, it is most costly. The theory of urban site rent stating as it does that rent does not enter into price will prove an additional damping factor, if of course the man intending to enter into business is a devoted student of Economics; because he will think that if it does not enter into price, he will have to bear it out of his pocket, if sufficient profits are not forthcoming. But that is not so. The mere presence of other shops, instead of being an inconvenience, is a factor adding to the importance of the place. Anyone going to the Hogg Market in Calcutta will feel that how can so many

shops doing the same business continue in one locality. The answer is obvious. Since so many shops are there—and there will be no objection if a few more are added—they have added to the importance of the place and attract customers from all parts of the city. Sometimes one particular locality in a town comes to acquire reputation for a certain class of trade. Any one intending to enter into that trade should select the site in the particular locality where the trade is localised. This localisation of trade is determined by several factors, *e.g.*, nature and extent of demand, reputation of the locality, nearness to the supply of sale articles, etc., of these the first one being of utmost importance. Another factor to consider in the selection of site is whether the importance of a particular locality is likely to change. It all depends on the shift of population, opening of railway communication, etc. If there is the possibility of any immediate change in the importance of site, it is advisable to open the shop in the neighbourhood of the area expected to prosper. Thus those people who had been far-sighted enough to open shops in the neighbourhood of the places where the Ganga Canal in Rajputana has been opened earned a lot owing to the reclamation of these plots where nothing was produced previously in the desert.

After the site is selected, it is necessary to make the shop as attractive as possible so that it may attract the attention of even a newcomer. This also adds to the decency and the customers also can feel a sense of pride in making their purchases from this shop. This requires careful attention in several respects, *viz.*, external decoration, window display, interior decoration and lighting arrangements. But then these are factors which may easily be copied from one's neighbour, and when one enters the Hogg Market in Calcutta, he can hardly make up his mind as regards purchase from any one particular shop, because in the matters mentioned above, all the shops maintain the same standard. Here therefore much depends on the whim of the purchaser and lot of the seller. But where the shops are not so much centralised as in the Hogg Market, a careful attention to the aforesaid factors is of importance in attracting customers.

Secondly, comes the organisation of the office. The size and nature of the office will depend on the size and nature of

the business and so also the degree of specialisation in office work. Thus if the transactions are too many, correspondences frequent and credit sanctioning abundant, specialisation would lead to economy not only in exertion but also in cost. In India however most retail organisations of the town and the village are extremely suitable, being managed by the owner himself, sometimes assisted by one or more hired employees, according to the nature of the business, but most often by his sons and other relatives. Even when an employee is taken, he is concerned with outdoor work, or distribution of commodities to purchasers coming to the shop, and the most confidential one being entrusted with cash and account-keeping. In many cases the work of correspondence is done by the owner himself in so far as he wants to preserve secrecy in these matters. The employees are all engaged on a fixed salary and the master's eye must be every where so that there may not be any scope for corruption. Rarely a share in profits is given; only in few cases profit is shared between all concerned, from the manager to the sweeper, according to the rank of each and importance of service rendered.

Another work of greater importance in connection with the office in retail trade is that of keeping record of every transaction. Many a concern comes to a sad end owing to its negligence in these matters. When transactions are on credit, the organiser cannot be expected to keep every thing in memory nor is it a wise policy to defer the work for some time. For, in that case, some items may be forgotten; therefore the work of record-keeping should be prompt and instantaneous. Not only that, every credit transaction should conveniently be checked and the mistakes rectified. Even when transactions are on cash terms, the need for record-keeping is not of less importance; for, it is from these records only that the shop-keeper can find out whether over a period of time he is making any profit or not, and take decisions accordingly.

Thirdly, the organisation of the stock room is also of importance; for, proper organisation facilitates greatest possible utilisation of the available space and speedy handling of goods and also avoids deterioration and pilferage. It also facilitates the work of ascertaining as to whether any particular article is in stock or not, where is it available and what quantity is on

hand. It also facilitates the study of the turnover of each article and placing of orders accordingly. Articles having speedy turnover should be ordered for in large quantities, so that there may not be any trouble with the customer. Articles having no or negligible demand for them constitute a deadstock, and care should be taken in their case, so that no deadstock may accumulate. If however any deadstock has accumulated, it is advisable that it should be disposed of at cheap rate and to realise whatever money is available; for their retention not only means the blocking of a part of capital in them, but also any possible waste or lowering of demand for them owing to change of taste and consequential further reduction in their price.

The characteristic of Indian retail trade as prevalent in most parts was the existence of trade guilds and caste associations from old days. These guilds had a striking resemblance with trade guilds in Europe, with this much difference that in this country heredity and not occupation was the unifying factor. As the Imperial Gazetteer points out, their object was the regulation of competition amongst the members by prescribing the days and hours during which work should not be done. The decisions of the guilds were enforced by fines and if the offender refused to pay, he was ex-communicated. If the guild contained men of different castes, it used its influence with other guilds to prevent the recalcitrant member from getting work. New entrants to any trade were made to pay a heavy fee and the income of the guilds was spent on feasts or on charity. Although in recent years a lot of changes has overtaken business yet the essential framework of the old guild continues in many parts in so far as the important sections of retail trade are closely knit in a *mahajan* or an association. Thus according to an enquiry in Bombay Presidency, there were 19 such associations functioning in Ahmedabad. In Bombay, however, only a few trades such as clothing, hardware, chemists and grain dealers are organised to a certain extent but then these organisations do not regulate conditions of work or wages of their employees, but are mainly concerned with disputes arising between their members and certain other matters. The membership of the Bombay Grain Dealers Association is composed of grain dealers and of retailers in

the grocery trade dealing in foodgrains. The membership is further divided into various local groups called *bazars* in different localities, each *bazar* having its own headman. The function of these *bazars* is mainly to decide which shops should remain open on days of closure like the *Amavasya* day when only a few shops are kept open for the convenience of the public. The Chemists' Association has a rule which requires that its members shall close their shops for half a day on every Sunday. Another tendency in Indian retail trade is the growth in the variety of shops. In the words of the enquiry, they "comprise such a large variety of different types of shops that unless they are combined into analogous groups, it would be impossible to draw deductions of any value." The most important ones of these shops consist of grocery and provisions, cloth and clothing, restaurants, and *bidis* and *pansupari*.

Large Scale Retail Trade—Departmental Store.

With the expansion of productive capacity and varied transport facilities, the distributive unit has also tended to expand in one of the two directions. Either there has been an enlargement in the size of the unit or, if the unit has remained the same, there has been a multiplication in their number. The departmental store represents the first type. From the standpoint of the lines handled, departmental store resembles a general store, being on a very large scale, and under one roof and central management, but unlike the latter, in so far as each line is separate from the other in immediate management. In England most stores, or nearly all of them, are not the result of any pre-conceived plan but merely the consequence of expansion "by stages either from the drapery establishment or less often from the grocery shop." In India the most well-known departmental stores are those of the Whiteway and Laidlaw and also the Army and Navy Stores, having their organisations in biggest cities, like Calcutta, Bombay. They are non-Indian concerns* and are the result of definite pre-conceived plan rather than that of evolution. In recent years some Indian concerns have also come into exist-

* Some of these have been purchased by the Indians in recent years.

ence, *e.g.*, Wachel Molla and Co. and the Kamalalaya Store in Calcutta, but in comparison with these non-Indian stores, they are still in their childhood and do not seem to have realised the need of emphasizing the aspect of service which is so vital in this line of organisation.

The selection of site is the most important in the case of the departmental store. Usually it is located in the central position of the big city and sometimes, as in the case of non-Indian stores in India in general, and that of Messrs. White-way & Laidlaw in particular, the structure of the premises is such that it cannot fail to attract one's notice, and incite curiosity. Inside also the stores are equipped with equal care, every detail being planned to ensure the greatest convenience, economy and decency. It is these things that often attract a passer-by and it is interesting that many people going inside the store are not all customers but have gone in to satisfy their curiosity and may in certain circumstances be converted into customers provided they are attracted by a particular commodity and they have means in the pocket to help them in getting hold of it.

The precise range of goods handled by a departmental store is extremely expensive and most progressive stores are every day expanding their activities in newer lines. The consequent advantage to the customer is that he can expect to purchase as many of the goods as he needs or most of them under one roof, instead of being required to move from one shop to another. But a factor of greater importance, particularly to fashionable customers, is that of service rendered by the store. Sometimes he would like to place orders over the telephone and be satisfied to receive goods at his own place. This requires that the store should have a delivery service as well, delivery being given free of charge. Some departmental stores have their own cars for the purpose, which also is a sort of advertisement. Sometimes the fashionable customer would like to give a personal visit to the store where his peculiar desire to receive a salute from the gate-keeper may be satisfied and where he may do his stopping at ease. Some stores therefore make it a point to establish special services departments for the convenience of their patrons, including the establishment of waiting rooms, restaurants, information

bureaux, telephone boxes, etc. The Indian stores have not emphasized this aspect of departmental store organisation, nor is it proper for them to do so at this stage of their development. If they spend a lot on these things at present, they may be involved in difficulties. The Indian stores are handicapped in this respect because of the small means of their customers. Since most Indian customers are men of limited means, the Indian stores would fail to attract them and secure their goodwill, even though rendering abovementioned services, if they raise the price of their wares a little so as to cover costs for these services. Their goodwill can be secured not by these services but by charging the price at a comparatively lower rate. The Indian stores, at least some of them, have realised this factor, while others who have not should do so, because, enjoying as they do the economies due to bulk purchase, they can, instead of spending a portion of their profits on these services, reduce prices a little, so as to attract the goodwill of the customers and when they have sufficiently stabilised their position, they should give some attention to the factor of service by spending a portion of profits for it, without at the same time sacrificing their original policy of selling commodities comparatively cheap.

The non-Indian stores are in a much better position in this respect. Their customers are restricted to the non-Indians and a very narrow circle of Indians having ample resources and not knowing how to utilise them best. So far as the non-Indian customers are concerned, they would do their shopping from these stores, even though they are to pay a high price, because of their *swadeshi* spirit to purchase goods manufactured in their home country and sold by concerns owned and managed by their own countrymen. So far as the narrow circle of Indians is concerned, they go there partly because they want to pass as fashionables and partly because they want to satisfy their peculiar sense of aristocracy by purchasing dear. The goodwill of these people can be secured by rendering "service", "free of charge", though the price of the commodity may be five times as high as that prevailing in Indian stores for the same type and quality. However, since as students of business we take the mental bend of customers as it is, there is need for provision for this particular type also and the Indian stores

may strive to explore possibilities of exploiting the demand of these customers, by having a separate, but side, store for them, catering goods at a higher price but at the same time rendering some services free of charge.

The departmental store is usually constituted as a limited company and in matters of constitution from the standpoint of law, it hardly presents any difference from other types of large-scale organisation. At the top there is a board of directors, consisting of persons most of whom may have little or no knowledge in the particular type of organisation, yet they have been taken in because of their success in some other line of business or because they are veterans having a wide range of experience. The day to day management is therefore entrusted to a managing director or general manager who is an expert in this matter. The board of directors is more often ornamental, framing and modifying policies from time to time. The centralisation of control in the hands of the managing director or the general manager should not be taken to be incompatible with the specialisation of the main activities by different departments, each of which, though under centralised control, is organic in itself.

The business of the departmental store is organised into several departments, the most notable of which are the technical department, merchandising department, sales department and finance department. It is the function of the technical department to examine goods on receipt, stock them, pack them at the time of delivery and to render similar other services. The life blood of the departmental store is however the merchandising department whose function it is to arrange purchases on most favourable terms from the most convenient sources and in correct proportions those particular lines which are in public demand, thereby obtaining economy in purchase and freight charges and also reducing the possibility of the accumulation of deadstock to a minimum. For this purpose there are experts studying the sources of supply, the competing lines of transport, the nature and extent of demand and allied problems, in the different lines dealt in and rendering advice from time to time to the merchandise manager. Purchase, as we have already seen, is the greatest problem, and due attention should therefore be given to it. The sales

department is concerned with actual sales, not only inside the shop, but also with the arrangement of local deliveries of goods and, if mail order business is also a part, with sending of goods from one place to another. In the Indian store business in Calcutta, the customers make the selection of goods from the particular department and hand over the money for them. There are some men moving with memo books, these men being common to several departments. As soon as the sale is effected, one of them is called for, who then receives payment and arranges for the change, if any, due by the customer, and gives a token, a part of the memo. On presentation of this to the packing department, the customer can get the other part of the memo and his goods from the packing department. A nominal inspection is made at the gate and one of the aforesaid parts of the memo retained there. The finance department is concerned with the financial aspect of the business, both receipts and payments. Sometimes there is a staff manager looking after the staff management. Only a few stores may have a management of buildings and equipments, the Indian stores, it seems, having no separate management for the purpose.

The rapid growth of departmental store in some western countries led many people to prophesy the ultimate decline of small scale retail trade. But their prophecy has not come to be true and the small scale retailer not only holds his own, but does so quite successfully in every centre of population, and although the volume of sale in a departmental store has been very great, yet when compared with the total retail sales, it is only a small proportion. In India, the field served by them is extremely narrow, being limited to some big cities and even there, as we have already seen, the Indian stores, although divided into several departments under one roof have sacrificed the fundamental principle of stores, *viz.*, service, and to that extent they may be regarded as only general stores on a large scale. Nor has the departmental store any very great prospect of success, in this country because the lack of personal element in it does not appeal much to the Indian population. Besides, the demand being limited, it is not possible for departmental store to hold its own in the interior. Only in big cities they may have some field for expansion.

Large-scale Retail Trade—Multiple Shop.

The departmental store represents one type of large-scale retail trade in which the unit of sales organisation assumes a very big size. Not so in the multiple shop system. This system is a compromise between the large-scale and small scale, combining as it does the advantages of both and striving to eliminate their disadvantages. It is a large-scale organisation in so far as it is placed under one management and enjoys the advantage of bulk purchase. At the same time, the unit of sales organisation is very small, as small as any other retail shop, speciality or general. The shops being scattered over a wide area can come into contact with consumers coming from surrounding districts of the locality. This is one of the methods in which the small retailer also may hold his own. When he finds that in competition with a large concern, he is being put to difficulty, he can extend his business by opening new branches. In this country, multiple shops in so far as they are to be found are not the result of the pressure of competition from bigger concerns, but are due to the desire of the proprietor of one concern to open new branches in different localities, thereby making a better utilisation of trade name and at the same time bringing services within the possible reach of consumers in different parts of a city, thereby pooling the whole, or a considerable part, of the total demand to themselves.

In England, there are three types of multiple shops. First, there may be a group of shops covering a certain district which are offshoots of one successful or flourishing central store. The proprietor of a successful business has employed his capital for the establishment of the new branches and as the number of such branches multiplied, the organisation in time became a fullfledged multiple one. Secondly, there are the more highly developed systems covering the whole country, the shops being supplied from one or more centralised warehouses and depots. And thirdly, there are systems in which the various branches have almost unlimited power of purchase and sale. The most common type of multiple shop in India, already noted, falls to the first category. This is to be found in many lines. The illustration of the second variety in this

country is the sales stores of the Bata products. In each store the supplies emanate from the same source and the shops, signboards, working arrangements, etc., for all of them are uniform. The unique fact about them is that they are scattered throughout the length and breadth of the country. In the third category, if we may say so, falls the concerns, like that of Messrs. MacMillan and Co., Publishers and Booksellers, having their central organisation in England, but the branches in this country having extensive power of procurement and sale. But so far as the true multiple organisation is concerned, the opening of branches by concerns in different lines is the only important one in this country, and that too is limited to certain big concerns of the cities.

In internal organisation, the multiple shop has some resemblance with that of a departmental store. The control in both the cases is unified under the managing director or general manager who keeps in touch with the activities of different branches through the medium of district managers and superintendents. In one respect however they may differ. The departmental store deals in various lines; the multiple shop may be a speciality one, dealing only in one line in all the branches. In fact, this is more convenient from the standpoint of management and control. If each shop resembles a general store, the management finds it difficult not only to arrange purchases for different lines for different stores in varied proportions according to the demand of the locality, but also finds it troublesome to exercise control over all of them. Within a limited range however multiple shops of general type need not cause any inconvenience.

Sales in multiple shops are almost in all cases on cash terms. For, since the people in charge of each shop are transferred from time to time from one shop to another, they can hardly find time enough to establish a direct and intimate contact with the consuming public, so as to enable the latter to seek goods on credit. This, of course, is not possible where only one or two branches exist and where, in view of the limited staff, transfer is rendered difficult. Whatever that may be, the financial control is exercised through the periodical sales reports to the head office, the reports showing receipts

and disbursements on various items of costs and the cash position at the end of the stated period.

The multiple conception has been carried to its logical conclusion by the fixed price chain store, a form of business organisation which has reached its height in the U. S. A. and is fast developing in England and some European countries. The fixed price chain store is a development out of one price shop, in which a large number of useful articles were purchased by a central office on wholesale lines and the location of the shop was arranged by the central office after close study and careful deliberation. The underlying principle of a fixed price chain store is the elimination of all slow selling lines of merchandise and absolute concentration on those goods which have a large demand in the market, the object being mass distribution of commodities. An idea of this mass distribution can be had from the following figures given by Florence E. Neal, already referred to in another context, for Messrs. Marks and Spencer who in 1930-31 sold through their branches $5\frac{1}{2}$ million pairs of artificial silk stockings, 6 million ladies' under-garments, 2 million jumpers and one million dresses. These figures are quite impressive when they are compared with those of any other type of distributive organisation engaged in the sale of these articles of merchandise. Just as in the field of production, production is carried on on a mass scale, in the same way, in the field of retail distribution also, business is carried on on a mass scale by the fixed price chain store.

The business policy of these stores makes an interesting study. As already mentioned, they restrict their work only to those lines for which there is already a large demand or for which they expect a large potential demand. This however should not be taken to mean that a fixed price chain store restricts its activities to a few lines only. In some stores of America the variety of goods actually handled is as many as ten thousand. But then all of them must satisfy the fundamental requirement, *viz.*, that they should have an extensive real or potential demand. The purchases for the chain-store are made centrally and in view of the large orders that they place, they keep very close contact with manufacturers and have a considerable amount of influence over them.

which is beyond the imagination of any other distributive organisation, including departmental stores. Sometimes, when they take all the products produced by the manufacturer, this influence becomes control, pure and simple, over the latter. Even when they do not depend on a single source of supply,—and this they often do as a matter of policy, for keeping more than one producer in the field, maintaining all of them by their patronage, while at the same time destroying monopoly in the field of production—still they can exercise a good deal of control in view of the fact that their patronage is the major determinant of the continuance of the producer. If the store withdraws its support and assumes hostile attitude, the producer would find it extremely difficult to get a rival concern for the distribution of its own products in view of the fact that the chain store, like an octopus, has kept the entire or a greater part of the distributive field in its own hands.

It should not however be apprehended that this commercial monopoly has led to an exploitation of the customer; just the reverse of it. For, the selling prices are deliberately restricted at a low level so that mass distribution may be facilitated. Another interesting feature is that the chain store is most often not concerned with the more expensive type of goods, for which, because of their very nature, the demand is restricted. The principle of standardisation which is so very important in chain store and which has been so very successfully applied to prices and supplies has been extended to as many aspects of the chain store as possible, for, it is even “extended to the architecture of the branches, their external appearance and internal layout all possessing a characteristic similarity. In size as well the individual branches are standardised so far as local circumstances permit.” No such instance of commercial monopoly, entirely independent of the producer and, in turn, exercising control over the latter, can be cited for India, so far as I can see.

So far about the chain store. A variant of the multiple shop organisation is the tied shop which in most cases, emerges as a result of financial difficulties of the tradesman already in business who, in return for certain financial or other assistance, allows the helper to exercise some degree of control over his business. The tied shop organisation however differs from the

multiple shop organisation proper in so far as the tradesman is not in the employ of any one but virtually independent, his hands being tied in certain respects only because of the financial obligations incurred. In such a case the trader strives to keep the fact of the shop being tied a secret from outside public, because if it leaks out, he would lose his reputation and credit in the market. A slightly different type of tied shop arrangement is to be found in case of agency concerns, where, of course, the tie is mutual. Thus, e.g., the agency firm may enter into agreement with the producer that the former would stock goods produced by him, strive to further their sale in preference to those of others and probably dispose of a specified quantity of the same within a certain time limit, in return, enjoying certain advantages and concessions from the producer in matters of credit, price of the product, or direct financial assistance.

Post Office as Intermediary—Mail Order Business.

The mail order business is an organisation which originated first in America in view of the vastness of the country. With the development of transport facilities and cheap postage, this sort of trade received a great stimulus in view of the fact that henceforth the people living at a distance or in the interior, could obtain their required commodities by merely dropping an order, at a nominal expense. Thus where the customer for one reason or another is obstructed from seeing the goods personally and handling them, this sort of trade is most suited. He may have seen advertisement for a particular thing, or received a free catalogue, or may have seen his friend or neighbour using the same; his desire to obtain a particular commodity is stimulated, what he is to do is simply to send orders by giving details, if any; and within a few days he will receive the goods at his own door at a nominal expense.

This sort of retailing differs from any other in all its aspects. As there is no need here for attracting the passerby, it has no necessity of having elaborate shop fronts, or window dressing or interior equipments. Since space is the barrier between the purchaser and the seller, there is no need for appointing a trained salesman. Nor is it necessary to make a

judicious selection of site, since site is no criterion here. What is needed at most is a warehouse, whose situation is immaterial, provided it is not far off from the post office or the transport facilities available. The necessity for the warehouse may even be obviated in those cases where the concern purchases goods on receipt of orders and may arrange for the despatch direct from the wholesaler, instead of bringing them into his own warehouse. What is needed at most is an office and some ordinary men to assist in the matter of purchase and despatches. These matters are so very simple that there is no need for the appointment of skilled labour but may be carried on in routine process by any layman. This is all the more so because the trader can arrange for an even flow of pressure of work on the staff. In the case of a retailer this is not possible, because at certain hours of the day, say, in the evening, he may have to meet the requirements of many customers at a time, while for the wholeday there may practically be no work. In the same way, at some period in the year there may be a greater rush of customers than at others. The ordinary retailer must be alert to the demands of all, and for that purpose, the salesman he should appoint, must also be equally efficient so as to be able to deal with many customers at a time to the fullest satisfaction of the latter. Not so in mail order business. It may so happen that at some time of the year, too many orders are rushing in. But it all is in the hands of the trader who can distribute the work of despatch over a reasonable number of days, thereby obviating any unnecessary pressure of work on the staff.

From the description given above, it may appear to some that the mail order business has the least elaborate organisation and therefore entails the lowest cost of distribution. The appearance is partially true or not true at all. It is of course admitted that the costs of distribution in this type of organisation are not of the same sort as those in the organisation of a retail trade proper. But, for the pushing of sale, an entirely different sort of expenditure has to be incurred; and therefore what appears to be saving at first sight is no saving at all and may in fact be a greater expenditure. Thus the costs of advertisement, postage, warehousing rents and charges and the return of merchandise sent on approval are by no means negligible but at times may cancel out any economies obtained in

other direction. This is not all. To make the mail order business a success is a task of much greater difficulty, in view of the geographical barrier separating the customer from the seller. Therefore, the seller must be shrewd enough to know the requirements of his prospective customers from a distance and issue advertisements accordingly so that the psychological weakness of the latter may be exploited and demand created. In this respect the task of an ordinary retailer is simple enough in view of his close contact with the customer or in view of the customer's personal inspection and handling of the commodity before purchase. It is well known that there are three types of customers—customers knowing their view when they enter into the shop, customers knowing their requirements but needing the attention of the salesman in the matter of choice and customers originally having no intention of purchase but afterwards having their interest stimulated in a particular article by one means or the other, and it is the last two groups that constitute the majority of shoppers. The retailer, coming as he does in contact with them, can win them over by a few minutes' talk; but the mail order businessman is in difficulty. So far as the first type of customers is concerned, he need not be worried. But in the second and third types, difficulty is enormous. His advertisements must be so effective that they can win over these two. That requires the services of experts in this matter, which is a costly affair.

In spite of its glorious beginning the mail order business has not developed to the extent to which it was expected to develop in the U. S. A. and in recent years it is showing a declining tendency. Some of the mail order concerns have supplemented their original business with chains of departmental or other stores, while some departmental stores have mail order business as a branch, placed under a department. In England, in view of shorter distances, this type of business organisation has never found a strong footing. In India, in view of the vastness of the country, the prospect of mail order business seems wide enough; but in view of the illiteracy of the masses, this type as an independent one is of little help. Where goods are sent per V. P. P., *e.g.*, in case of books, this sort of retailing is only a part of ordinary retailing or wholesale trade.

Consumers' Credit—Hire Purchase System.

In economic literature a distinction is often drawn between demand and effective demand. There may be demand for a particular commodity; but unless it is backed by purchasing power, it cannot be regarded as effective. Therefore, some devices were sought to be discovered by which the people, who have demand but who cannot make it effective, can satisfy it without at the same time being strained. The retail trade organisation that we have discussed so far is concerned with the man with a rupee in the pocket. They do not care for those whose pockets are empty. So the device which sought to remove this inability of a certain section of the population is known as consumer's credit, which implies loans of money or sale of goods in time to individuals who use the money or the goods in satisfying their daily wants. Consumer's credit, it is interesting to note, is a neglected device so far as the banks are concerned, for, under modern banking system, consumer's credit, as distinguished from investment and commercial credit, has no place in any country, India being no exception. A certain amount of trade credit is however extended by retailers in villages and towns, to a particular section, specially the government officers or others having a fixed monthly income who receive goods on credit and settle accounts once a month after they receive their salary. But there is no organised institution for the purpose of advancing consumer's credit.

A recent development of consumer's credit is the introduction of hire purchase system. In a hire purchase system, the proprietor of the concern offers to the customers articles whose prices are too high to be paid by them in one instalment. The payment is therefore to be made in stipulated instalments over a period of time. This payment in instalments should not however be confused with instalment trading. In case of instalment selling, a certain amount of payment is required on the delivery of the article, and the balance is paid off in weekly or monthly instalments. It is the peculiarity of instalment trading that under it the article is sold out and therefore cannot be returned, and the instalments must be paid. If the purchaser finds it inconvenient to hold it, he can sell it off at his discretion. Not so in hire-

purchase system. In a hire-purchase system, the article being hired, the person, possessing and using it, is not its full owner; he has simply hired it. Therefore, he cannot sell it out and if he does so, he commits a criminal breach of trust and the seller can recover the article from sub-buyer. In a hire-purchase system, a certain amount is deposited with the seller and further weekly or monthly instalments are paid in accordance with the terms of the contract.

There are two limitations in the way of the success of hire purchase trading. In the first place, the hire-purchase system can be successful only in case of persons whose credit and ability to pay are sufficiently well-known. As such it is mostly confined to persons with a fixed income or to salaried classes. This being so, the very object of consumer's credit, *viz.*, granting of credit to those who cannot make their demand effective by making payment for a thing at a time, is frustrated, in so far as it is limited within a section of people who are sure of their income. And secondly, there is the possibility of the trade being too much reckless in the granting of credit, and unless proper care is taken, it will involve the whole trade in disaster. In India, the hire-purchase trading is limited to the sale of expensive articles like motorcars, typewriters, sewing machines, furniture, costly books, etc. and is apparently restricted to the well-to-do circles of the towns and big cities and has not spread to urban and rural areas. The suggestion for the supply of agricultural implements to the agriculturists on hire purchase system is an old one, but does not seem to have made much headway in this country. The expansion of the hire purchase system would help a very large section of the population in this country.

In countries where hire purchase trading has developed considerably the concern often finds it difficult to provide capital. Therefore finance corporations have been founded with a view to assist them. It is the function of these finance corporations to buy the hire purchase agreement from the dealers, either with or without their endorsements and undertake to collect the instalments on their own responsibility. These corporations charge a certain percentage by way of their own remuneration of capital advanced and services rendered. Where the dealer gives his endorsement on the agreement, the

risk of non-payment is shared between the dealer and the Corporation, in which case the charge made by the latter is comparatively less. When, however, the risk is not shared but is undertaken by the Corporation alone, it retains a larger percentage on loaned amount towards its charge or profit, as a reserve against bad debts and as remuneration for the trouble of collecting instalments. This reserve is frequently returned when the Corporation has realised its money.

Another form of consumer's credit, known as club trading, has assumed diverse forms and has become very prominent among the poorer population of the chief industrial areas in England. The most common type of club trading is one in which the member receives goods he wants to purchase before the full payment has been actually made. It is interesting to note that although this type of trading is limited among the poorer sections, who are most likely to create trouble at the time of payment or may refuse altogether the payment, yet the extent of bad debt in this type of trade is "surprisingly low." It also depends on the sense of morality of the members, which alone is a secure foundation for this type of trading.

Pricing under Retail Trade.

A study of pricing under retail trade would be of interest in view of the fact that it is the retail trader who charges a price which comes out of the pocket of the consumer. This is the last transaction in the chain and all the previous purchases and sales were mere efforts at pushing the thing to its destination. At each stage of transfer, certain items of costs and profits are added. The retail trade is not an exception to this. Had the matter been this far and no farther any separate study of pricing would have proved superfluous. But as will be seen presently from some sample examples, price of the same commodity becomes different according as the seller belongs to one or the other of the different types of organisation. The only expression of pricing under retail trade in classical economic literature is to be found in the writing of Taussig, according to whom retail prices are governed by custom. But this sort of too simple a statement is worse than none. The correctness of a general statement of this character can to some extent be

found in the interior markets of our country where the petty shop-keeper most often does not keep abreast of current developments and so long as the stock in hand is not exhausted, he will not like to change the level of prices he has fixed, no matter how very great may be the fluctuations in wholesale prices. When his stock is exhausted and he has to purchase the same at a higher price, he may raise the price if his competitors do so and the demand for the commodity is inelastic; but he must do so if the change continues over a long period or is a permanent one. In case of a fall in prices, he will not in ordinary circumstances like to lower it, for the low prices may be short-lived and when raising again he may have to face tremendous opposition from the consuming public. To this extent therefore price is governed by custom. It must however be admitted that in certain instances the hold of custom on prices has proved so very important, that it has often been thought to be a wise policy to change the quality and/or size of the package of goods rather than bring a change in price. This sort of adjustment is very common in case of articles popularly used, *e.g.*, tea or tobacco.

But custom is not the only factor, and a thousand other considerations creep in before the price for the commodity, so far as the customer is concerned, is determined. It is interesting to note that economic theory is incorrect in so far as the price is the last thing to be determined by a market process. The price is already calculated by the seller, and marked on the face of the commodity or on the cover either actually or in cipher; the customer must either be ready to pay the price as demanded if he wants to get possession of it or simply to quit. The practice of charging an exorbitant price and then as a matter of higgling lowering it slightly, but still having it much higher than the actual cost price is now gradually giving way to a fixed price, whatever that may be and however that may be determined. The retailer, in calculating the price is mainly influenced by the following factors. The first factor to be considered is the costs of goods—costs of production and also costs of distribution till it reaches the retailer, supplemented by the working expenses of the latter. The calculation of costs till the arrival of the goods to the retailer's shop is quite a simple task; the retailer has already paid them and therefore

they are already calculated. But a great amount of difficulty presents in the calculation of working expenses, which in many cases are calculated, at the end of each year, in a rough-and-ready manner. This is one of the greatest imperfections in the determination of prices, for the working expenses added to the price are not the actual expenses but what the retailer thinks them to be, and most often he will think them to be more instead of less, particularly so when there is no competition between different retailers or when all of them adopt a standardised process in this respect. The actual working expenses are not the same for different retailers handling the same line of wares. They vary with the services rendered, risks undertaken and sales turnover. Where more elaborate sales services, including delivery services, are maintained, the working expenses will increase, though not proportionate, to a certain extent—to what extent, will, of course, vary according to the volume of sale. Thus if as a result of the maintenance of sales services, the volume of sale increases, the cost incurred by the retailer for them is distributed over a greater number of articles. It all is a question of turnover; the greater the turnover, the less will be the cost per unit, no matter whether the total cost as it may seem very high. Working expenses also vary according to the risks undertaken, though this factor is not of major importance in retail trade in view of the fact that a greater part of the risk is borne by the producer and the whole saler. But yet, in view of the limited resources at his disposal, the risks undertaken by the retailer, though apparently small, are not negligible from his standpoint. Thus if as a result of a sudden change in demand, the stock of a particular commodity has become blocked, he cannot but strive to incorporate the loss in working expenses and realise it in the price of other commodities. But then he cannot charge a price different from that charged by his competitors.

Secondly, the quality and reputation, two incalculable factors, enter into price determination. Thus there are some customers to whom a commodity of high price is qualitatively superior, though there can be no logical connection between high price and quality. It is all a question of psychological satisfaction. These customers do not, and in fact have not the capacity, to examine the true quality; they are simply satisfied

because since they have paid a high price, the commodity cannot but be good. The economist would say that these are abnormal people and therefore need not be studied; the businessman knows that they are not a rarity. In the same way, there are some commodities which have long been in use and have been kept up in public estimation by continuous advertisement; and even when a superior type of rival comes into the field at a lower price, it may find it difficult to compete with the high priced article. This is invariably the case with products coming from a new concern, unless the latter happens to be an all-ready reputed one, backing the distribution of the goods by the wide range of propaganda.

Thirdly, the price policy of the retailer is a determinant, nay, an important one. Thus when payment is made in cash, the policy pursued by the retailer would be quite different from that when goods are sold on credit and payment will be made by instalments. In order to stimulate cash transactions, retailers are often found to give a rebate or discount, or other inducements for cash transactions. The granting of these concessions is to the mutual advantage of the seller and the customer—the seller, because not only cash transactions but also turnover are stimulated, and the customer because he gets the commodity cheaper and sometimes is rewarded in kind. In England, some of the shops have adopted “dividend stamp” scheme. For every cash purchase certain number of stamps are given which increase as the money spent on purchase increases. The customer is provided with a book in which these stamps are to be affixed. When the book is filled, or a definite portion of it, according to the conditions, goods to a specified value may be obtained from the shop without further charge. In case of instalment system, however, since the price is paid over a period, higher price is charged for covering the loss to the seller due to his money lying idle. An intermediate system is to be found in case of some concerns supplying electricity who grant credit for a short period and also a rebate if the payment is made within a specified date.

Fourthly, different prices are charged by retailers for the same type and quality of commodity according to the difference in their organisation. This point we have already clarified in

connection with the discussion on departmental store where it was seen that prices vary because the customers, instead of shopping in this quarter of the town, has selected that quarter and instead of shopping in this store has selected that one. It may often be said that high price is charged, say, in a departmental store because of high services rendered; but it is questionable whether the high prices are in keeping with the extent of services rendered. Probably, the high prices are charged, not because of high costs nor because of elaborate services, but, as in the case of first class railway fares, simply to entrap a certain class of customers who have ability to pay and therefore must pay, and also, probably, the store wants to shut out the ordinary customers. The precise explanation from economic standpoint is possible in this case. On the contrary, in the case of fixed price chain store, where business is carried on on a mass scale, both purchase and distribution,—probably on a larger scale than in case of departmental store—goods are disposed of at a lower standardised price. The self-imposed limitation of a departmental store by its peculiar price policy for the same sort of goods stands in marked contrast to the policy pursued by the chain-store. In this case therefore, the particular type of organisation and sales policy are the determinant of price.

Thus it will be seen that from the standpoint of the retailer as also that of the ultimate consumer no single explanation of price determination is possible. It varies from commodity to commodity according as one is in use over a greater period and backed by good advertisement, from one store to another according to their organisation and sales policy and from locality to locality according as one is frequently visited by the fashionables and the other not, and from one district to another or from one province to another owing to lack of information, mobility, etc. Sentiment also plays a great part when an Englishman is purchasing goods from M/s. Whiteaway Laidlaw and an Indian a piece of khādi even though both are ready to pay, and actually do so, a higher price, with this mental satisfaction that they are doing their best to support home industry. No less important role is played by tariff in the determination of price. When America goes protectionist, she helps the maintenance of high prices within tariff walls,

which under ordinary circumstances would have gone down. When England goes off gold, she deliberately lowers the price of her exports so that effective competition in world market may be rendered possible. These and a thousand other factors, visible and invisible, determine prices and any theoretical formulation which fails to incorporate all those—and they must apparently fail to do so—are worse than no formulation at all from the standpoint of business; the so-called dynamic theories are not sufficiently dynamic so as to incorporate all these factors.

We have noted above some of the elements that determine the price policy in retail trade. A new problem has however been created owing to the recent monopolistic tendencies in this field. For long this monopoly presented itself in the form of patented goods. But the manufacturer of to-day has gone a step further. He is not merely satisfied with the legal protection given by the patent office but tries to exploit to the fullest extent the psychological weakness of the consumers by branding the goods and thereby establishing a permanent reputation and capturing the goodwill of the customers. He is not merely satisfied with the determination of price at which he will sell to retailer but is equally interested in the “resale” price, *i.e.*, the price at which the commodity reaches the consumer. In such a case the price system loses its elasticity and its place is occupied by a rigid system of price control and price uniformity. This regulation is of two types, *viz.*, in the first place, that exercised by the manufacturer in the form of branding of goods and thereby fixing their price, and in the second place, by the retail trade itself which, through some organisation or other, exercises control over the margin at which the members of a particular retail trading group should sell their wares. It is very difficult, at this stage of the development to pronounce any judgment on this new control. Only time can show, particularly so when this type of controls and regulations are not yet widely extended in this country, whether they are beneficial in the interest of the consumers. But one thing is certain. The age-long assumption that the forces of demand and supply determine price and regulate its movement must to-day be discarded in favour of one in which price is being regulated by certain monopolistic groups, both

in the field of production and distribution, by their control over supply.

Thus we are living in an economic system in which price of articles—at least branded articles, and they are increasing in number—is determined beforehand and not left to the market forces nor to the business position of the retailer. Previously, when the rule of branded goods has not come into existence, the price that the retailer charged may in some circumstances have been determined by custom but mainly it was determined according as what the market was in a position to bear. The retailer made his purchases at the lowest possible price and tried to realise as much as he could on them according to the circumstances of the market. Thus his bargaining position determined his profit. Not so to-day. Most of the articles in which a retailer deals are branded goods with prices fixed by the manufacturers. His margin or discount, whatever that may be, is determined in the one case by his trade association or by force of competition among the retailers themselves and in the other by the manufacturer. The only way in which the retailer can expand his profit total is only by effecting an increasing turnover. This fact all the more shows why effective salesmanship, which is the only way of increasing turnover, is so very essential in present-day retailing.

The present-day retailer is therefore interested in two things, first the turnover, and second the margin. Turnover is a matter which depends on the demand for a particular commodity from the customer, which in its turn is influenced by the price fixed by the manufacturer. If the retailer in a particular locality is not satisfied with his turnover, what utmost he can do is to give up his deal in that particular ware. If however the reaction of the whole market is unfavourable, the manufacturer must either improve the quality or lower the price. But generally these factors receive the consideration of the manufacturer before the price is so fixed and he is little affected by the grievances of a particular retailer, unless the grievance happens to come from some strong trade association. The other factor in which the retailer is interested is the determination of margin. This determination of margin is also a complex task. But in the main it is influenced on the one hand by the position of the manufacturers and on the

other by that of the retailer and also by the nature of the demand. If the commodity is one which is largely demanded by customers and the retailer cannot do without it, in that case the producer is in a strong position and if the producer raises the price that he charges from retailer, the retailer will be in a delicate position to forego a part of his margin rather than to give up his deal in that particular commodity which is in so high a demand. One interesting case is noted by Hermann Levy in his *Retail Trade Associations*. In 1906 Messrs. Lever and Co. announced an increase in the price of soap to retailers, which would have reduced the margin to retailers from $17\frac{1}{2}$ p.c. to $12\frac{1}{2}$ p.c. "This was a demonstration of the firm's strength and of the favoured quality of its products, which had almost acquired monopoly value; the retail trader was to bear at least part of the burden, for 'Messrs. Lever refused to raise the retail price.' " Where the producer is not in so strong a position, but some sort of combination exists among retailers, the latter will exercise its influence on the determination of margin. At times the organisation of retailers may combine with the producer on some matters of pricing and thereby may have its influence on price policy. At times where this organisation is sufficiently strong, and the producer's position is definitely weak owing either to the existence of limited market or to the competition of rival firms, the latter is guided by the former in this matter. Where however, the producer is in a strong position either because of reputation and goodwill that he has been able to earn or because of concentration of production in fewer firms, the retailers' position tends to be delicate and his margin consequently small.

A further difficulty in the determination of margin is presented by the fact that conditions in retail trade are least standardised and therefore the cost items in different types of retail trade organisation are different. Even in a country like America which is well-known for standardisations and where the administration also is very particular in these matters, the problem has not yet been adequately solved. In other countries the condition is still very backward and hence the difficulty all the more great.

A few words may be said about the margin in the Indian

retail trade in case of agricultural produce. Unlike in case of manufactured products, the margin in case of agricultural products shows wide divergence partly due to the "extreme variability" of the product and partly due to "the process of bargaining which accompanies almost every transaction." In the words of the *Report on the Marketing of Rice in India and Burma*, "Retail prices are never marked on the articles offered for sale and the first price asked by a retailer is generally put forward more as a basis for argument than as a serious quotation. It is also common experience that the appearance and status of the prospective buyer is an important factor in determining the price to be asked. In other words the quotation is based on what the customer is estimated to be able to pay." But for those agricultural products, or at least those varieties for which competition is very great, the margin naturally declines and in some cases may even become negative. As standardisation of agricultural products will take place, this complexing variability as also the confusing and at times artificial multiplicity of nomenclature will give way and margin will be regularised. With the increase in the number of retail trade associations and with the extension of the areas served by them also, a helpful development in this line is likely to take place.

Much has been said on branded goods and price policy with regard to them. But even in case of those goods which are not branded, the price at which the retailer sells comes to be fixed by force of circumstances and price maintenance then becomes the rule. In fact, price cutting by any retailer is treated very unfavourably by his fellow tradesmen and has also received indignation from the very many writers on retail trading who have gone so far as to regard it as "anti-social activity." They have not altogether neglected the factor of efficiency. Thus if the price cut is due to increased efficiency of any businessman, it is not regarded by them as anti-social. On the contrary, this particular trader "is entitled not only to the admiration of his competitors, but to the thanks of the public as well." But "any man who, at the expense of his fellow merchants or manufacturers, persistently sells any article without taking a decent profit is like the cheating golfer. If everybody followed his example, as he knows well

enough, the whole commercial structure would smash to hell." The United States has gone to the extreme in the matters of price maintenance because in some of the states sale below cost is regarded as unfair and the judiciary has given its decision against such practices in some cases. Maintenance of price was also one of the important and interesting features of the United States N. R. A. codes.

But one thing should strike at this point. Is it possible for any retailer to sell below cost permanently, unless the price at which he is selling is above the cost that he incurs, leave aside the case of others? If that is not so and if this "sale below cost" is rendered possible because of his increased efficiency, the expediency of any legislation against such practice can and should be questioned. If however this reduction in price is not due to real increase in efficiency but a case of price cutting pure and simple, even then there is no need for legislation, for such procedure cannot go on *ad infinitum* and the seller must either fall in line or be ousted.

There are cases, again, when price reduction is a definite policy. Take the case of clearance sale at the end of the season. If they follow the policy of price maintenance, they cannot attract the same number of customers and they must carry some stock till the next season at the risk of their being spoiled. Or take the case of different editions of Tagore's books. Some are sold at a high price while others containing the same thing are sold at a low price, these being the popular editions. There are certain publishing concerns who are bringing out some of the old famous books at a very low price. It cannot be said that price maintenance should apply in these cases. Thus it is clear that price policy in retail trade is not the result of the two economic forces of demand and supply alone, but also of various non-economic factors, as also of factors connected intimately with the type of business organisation.

Importance of Salesmanship in Retail Trade.

The importance of salesmanship in retail trade need not be emphasized. We have already said that the retail trade is

the one which comes into contact with the consumer. In the previous stages, no salesmanship is called for. The wholesaler obtains goods from the manufacturer, either direct or through agents, and so also retailers. In so far as the agents deal with the wholesalers and retailers for inducing them to purchase a particular line of wares, they work as salesmen. But the precise nature of their work is quite different from that of the ordinary salesman in a retail store. In the first place, the agents have to deal with a limited number of persons and firms and secondly they are dealing with those who must purchase some line of products for their business. Not so in case of a salesman. He is to deal everyday with innumerable persons, some of whom may be mere visitors satisfying their vacant curiosity while others have no fixed demand but may purchase something if they are induced to do so. Here arises the need for salesmanship which is a great art in the field of business.

According to Houghton, salesmanship is an "art founded on the principles of economics and psychology." It is the function of the salesman to bring these two factors together with a view to the attainment of a certain objective, *viz.*, effecting sale. The economic principles are those which are applicable to man in his economic life where he is guided by the motive of "getting a living." But mere getting a living is not enough and is followed by its distribution over various needs which is determined by the needs of the man, the means in hand and the relative urgency of the needs, these all being determined by the psychological make-up of each individual. Here comes the application of art and an expert salesman is to study the behaviour of each individual and exploit him accordingly. The more accurate this study of behaviour, the greater the degree of success attained by the act. Houghton has given a very nice simile. "You can think of the art of salesmanship as a fabric of interwoven strands. A piece of cloth is made up of strands which are woven together. The warp consists of those which traverse the length of the cloth and the weft consists of the shorter strands which traverse its breadth, and, to a great extent, determine its pattern. The art of salesmanship can very well be compared with a pattern of cloth. The warp represents those principles of economics, the weft

Fashion.
History and general reputation.
Social values.
Special terms of sale, guarantees or continued service terms, hire purchase terms, etc.
Convenience.
Ease of use.
Value in relation to other articles of similar character."

The salesman must be familiar with these selling points, which is of absolute importance in winning over the customer and bringing about his satisfaction.

In Western countries,—in some of them at least,—systematic training is given to salesmen. A comprehensive course is prescribed for and, before a salesman is appointed, he has to be fully trained. In this country no such systematic educational facilities have been arranged. Whatever is learnt is learnt because of long association, sometimes from the very childhood, with business. But those who at an advanced age take a decision to work as salesman cut a poor figure when appointed in a concern. The so-called commercial education imparted by men having in most circumstances no idea about the practical field is extremely helpless, particularly in matters of salesmanship, which, being an art, requires a practical handling of customers and not a bookish knowledge about it. The system of keeping apprentice or being appointed as salesman seems to be the only solution, which, if associated with systematic training according to the requirements of handling Indian customers, would be of immense benefit to the future trade of India.

With the development of the press and postal facilities, another form of salesmanship has come into being, *viz.*, advertisement. It differs from salesmanship proper in so far as the appeal to human psychology is of an indirect type. In salesmanship the appeal is made direct to the customer, and that too one at a time; the wordings of the appeal can be modified according to the requirements of the situation. In advertisement, appeal is made to a large number of persons at a time and the appeal is repeated, may be in different words, so that

it may create some impression on the readers. In Western countries, this method of appeal has gone so far that articles are sold most often, not by the direct appeal by salesman, but by the brands familiarised through the medium of advertisement. So far as India is concerned, advertisement cannot be regarded as a very effective weapon, mainly because of the prevailing illiteracy. Most customers in the interior and many in big cities need the attention of salesman. There is another obstacle as well. For, the foundation of advertisement, *viz.*, branding of goods and registration of trade mark, is rather weak. There is no provision for the registration of the trade mark, the priority in use being given to one who is already using it. But it becomes, at times at least, extremely difficult to prove this priority. At times again the same or similar brand may be used by more than one concern, the others benefiting by the advertisement of one. With the growing literacy, this medium will assume increasing importance in this country as well.

*Reaction Against Capitalistic Retailing--Consumers'
Co-operation.*

Consumer's co-operation is a reaction against capitalistic retailing, having as its object the elimination of middleman and his profit. In this respect the lead came from Great Britain which maintains the biggest store—the Rochdale Pioneers. "One may measure the stores of other nations by the degree in which they fall short of the English model; for it is the measure which they themselves apply." The objects of the pioneers were defined as follows in the original rules.

"To form arrangements for the pecuniary benefit and improvement of the social and domestic condition of its members by raising a sufficient amount of capital in shares of one pound each to bring into operation the following plans and arrangements:—

"The establishment of a store for the sale of provisions, clothings, etc.

"The building, purchasing or erecting of a number of houses, in which those members desiring to assist each other

in improving their domestic and social condition may reside.

"To commence the manufacture of such articles as the society may determine upon for the employment of such members as may be without employment or who may be suffering in consequence of repeated reduction in their wages.

"As a further benefit and security to the members of this society, the society shall purchase or rent an estate or estates of land, which shall be cultivated by members who may be out of employment or whose labour may be badly remunerated.

"That as soon as practicable, this society shall proceed to arrange the powers of production, distribution, education and government; or in other words to establish a self-supporting colony of united interests or assist other societies in establishing such colonies.

"That for the promotion of sobriety a temperance hotel be opened in one of the society's houses as soon as convenient." The fundamental features of the Rochdale system of co-operative store are two-fold—sale of commodities at market price on cash terms, and distribution of profits among the members in proportion to their purchases.

The central management and administration of a co-operative store are vested in the members, in a committee formed by members and the officials of the society. It is the function of the committee to formulate the general policy of the society and it is for the members to consider and criticise and thereby influence and mould the policy so formulated. Another function of the committee is to supervise the officials of the society in the execution of their functions. In the case of a big store, the committee may appoint a number of sub-committees to look after the work of different departments. The day-to-day working of the societies is looked after by a general manager, who is an employee of the society, assisted, if necessary, by branch managers.

In matters of purchases, the committee of the members plays a very important role. With the expansion of the store, however, this function has to be delegated. For, where purchases are considerable in volume and value, a greater degree of specialisation would lead to convenience, and economy. Not only that, purchases in present day economy need considerable technical knowledge and information which are

beyond the capacity of the members of the store, most of whom have no knowledge of the technicalities. Often the purchase policy is determined by the general manager; but in a big co-operative store this may be delegated to a special department consisting of experts in the matter. But the co-operative stores are in a disadvantageous position as compared with the capitalistic retailer in one respect at least. For, the committee would require that all or as far as practicable the purchases must be made from co-operative wholesale society or any other co-operative sources, any purchase from outside sources being made only when the former are not in a position to supply. This aspect of the problem has been of special importance in this country in view of the inadequate development of co-operative sources of supply. Even to the small extent to which the store movement has developed in this country, at times and in some provinces it has found it difficult to obtain supplies from such sources and has been compelled to tap other possible sources, more particularly to purchase direct from the producers. This, it is natural, is viewed with great concern in co-operative circles. But in the present stage of the development of co-operative sources of supply, their unorganised character and their inability to supply guaranteed quality of articles at competitive prices, it is too much to expect the store movement to be organic in character. In the present stage of its development, it cannot disturb the loyalty of its members by its efforts to patronise the undeveloped and inefficient wholesale societies and cater for the needs of the members with less efficiency and at higher prices. The structure of the store movement in this country is as yet too weak to be able to withstand any compulsion in this respect. But then if the co-operative sources of supply do not get adequate customers from their brothers-in-faith, it will not be possible for them to pull on. Under the stress of wartime conditions, a greater degree of co-operation is visible between the two. But with the end of the war the conditions would change and if the wholesale societies are unable to bring about improvement in their working, it would be extremely difficult for them to pull on. Therefore, ways and means should be thought out from now so that the small amount of co-ordination that has been possible may continue and develop still further.

Another controversial problem connected with the co-operative stores is that of price fixation. We have already examined some samples of price fixing in capitalistic retailing; in co-operative retailing the problem is slightly different owing to the fact that business in this case is performed not for profit but for mutual benefit. Hence the problem centres round the question of the percentage which shall be added to the costs of production and distribution in order to cover the working expenses and allow a reasonable profit. We have already seen the difficulty in calculating working expenses which vary from concern to concern. No less disputable is the question of determination of the reasonable rate of profit. So far as the latter is concerned, much depends on the desires of the members. They may want to have the goods at low prices—lower than the prevailing market prices—and be contented with a nominal dividend; or, they may be prepared to pay equivalent to the market price, but desire to have higher dividends declared. But here arises another conflicting consideration. As already mentioned, the making of profit is not the co-operative ideal and its success is to be measured not by profits derived and dividends declared, but by the services rendered for the benefit of the members. Nor is it at the same time wise to supply goods at a price lower than the prevailing market price, for that brings about an unnecessary conflict with capitalistic retailing. That is why the principle under the Rochdale system is to sell at the market price and grant a rebate on purchases, so that it does not conflict with the co-operative principle of not making a high profit, while at the same time it avoids unnecessary friction with capitalistic retailing. At times the utilisation of capitalistic methods, e.g., granting of rebates which is generally used to push sales and encourage cash payments, with a slightly different objective, the technique, however, remaining the same, is essential for the stability of the economic structure.

Since the objective of the co-operative store is to look after the interest of the members, one principle should therefore be followed in matters of price fixation. It is well-known that owing to the operation of the various economic and non-economic factors, prices in capitalistic market fluctuate vehemently and though the retail prices are more or less stable, yet

they are not altogether immune from the effects of such fluctuations, and when speculative spiral is high, the private merchants may be profiteering, by charging high prices either direct or by bringing pressure on consumers by withdrawing supplies. The co-operative store should however not deviate from the principle, and join with the speculators. The position evinced by the stores in India seems to be extremely weak in this respect owing to their almost absolute dependence on capitalistic production and intermediaries of supplies. This dependence, unlike that in England, has been the cause of the failure of the Indian stores even in provinces like Madras where they have made great progress comparatively, to influence the market conditions and they have in actual fact followed the latter. "Either it (stores) should produce all such goods itself or should assist in the formation of co-operative producers' societies from whom it can get all its supplies."

Another important point connected with the sales policy is that of credit sanctioning. It has often been asked whether sales by co-operative societies should be made on cash terms or on credit. Credit undoubtedly is the basis of modern commerce. But as far as co-operative store movement is concerned, the spirit and principle are quite clear. Its object is not the same as capitalistic commerce. Most often its activities are limited to members; even when the non-members are attracted, the point of attraction should be, not credit, but low prices. Therefore, trading on credit has been opposed by the veteran co-operators. Whatever that may be, even in countries like England, "the societies have been compelled to sink their principle in order to gain a footing." In India, however, sales should be effected on cash terms; for, if credit is encouraged, the movement will be nipped in the bud. Even when the movement has sufficiently progressed, insistence should be placed on cash transactions.

When we speak of co-operative stores in this country, it should not be taken to mean that there is any such thing as a store movement on a large scale in this country nor should it be conceived that the stores supply a greater part of the needs of the members. In most provinces it has made only a humble progress and in others the progress is negligible. Even in Madras, which may be regarded as a natural home of store

movement, "the history of consumers' or distributive co-operation in this province, with the single exception of the Triplicane stores, has not been a record of success." The earlier difficulties in the way of the store movement have been legal in view of the fact that the stores had to combine credit in order to get themselves registered under the Act of 1904. The association of credit with sale cannot however be regarded as a sound principle in the early stages of the store movement, particularly so when many of our credit societies have been suffering from the accumulation of overdues. The organisation and functioning of the stores were also no less defective. "Some of the stores suffered by wrong location. Purchases were not made in the proper centres, in the proper seasons and in sufficient bulk. Prices paid were, therefore, unfavourable. Working capital was insufficient for stocking goods; and the Central Banks were not, generally, inclined to help the stores to buy in bulk and stock in advance. There was not enough business talent among members of the managing committee; if there was, it was not dissociated from self-seeking. Due to lack of workers with leisure and inclination to do sustained work, paid staff had to be appointed for every kind of work and that added to the overhead costs which had to be spread over a limited quantity of goods. The margin that obtains between the wholesale and retail prices is much too small in our markets, where there is cutthroat competition among dealers who are far too numerous for the volume of business done. The violent fluctuations in prices between the time of purchase and that of sale in certain years forced some societies to close down. The depression hit hard every kind of institution and the store had its share of troubles. Members found it more and more difficult to purchase for cash. The permission given by the Registrar to societies to sell on credit up to half the salary of a member was not of much avail to many. In fact there are few towns where a large clientele could be found with a steady and substantial income to be depended upon to be ever loyal to the society. The salaries of most of the middle class educated men in towns are lower than the wages of the better type of working classes who are the backbone of the urban consumers' stores in industrialised countries and even of the rural stores in Denmark." (*Year*

Book and Directory of Indian Co-operation, 1942). This is a fairly extensive list of the defects and disadvantages from which our store movement suffers even in Madras. The picture in other provinces is all the more precarious.

In recent years, however, the store movement has made slight progress, and the "new impetus to consumers' co-operation after a long period of comparative stagnation" has been due to wartime developments. But this must not be taken to mean that stores have cropped up throughout the country; nothing of the kind. Whatever development has taken place is restricted mainly to Madras Presidency. The lines of development in that province have been varied. In the first place, there has been an enormous expansion of rural primary co-operative stores, as is shown in the following figures:—

(Source: *Eastern Economist* 14. 2. 47).

	1938-39	1943-44
Number of Co-operative Stores	... 21	713
Number of members	... 2888	110164

(In thousands of rupees)

Share Capital	... 17	1619
Borrowings from Co-operative banks	... 23	3198
Borrowings from other sources	... 18	1762
Total Borrowings	... 41	4960
Borrowings outstanding due to		
Co-operative banks	... —	1475
Borrowings outstanding due to others	... 7	794
Total Borrowings outstanding	... 7	2269
Total Working Capital	... 56	4062
Total Purchases	... 328	19122
Total Sales	... 351	19648

The causes of this enormous expansion are so many. Since supplies are limited and markets controlled, the need for efficient management and effective salesmanship is not so great. The customers accept anything they are offered. The stores are relieved of so many other functions that are very essential in peacetime, e.g., collection of market intelligence, knowledge

of sources of purchase, etc. The increase in the purchasing power of the rural population and the extension of clientele to non-members have been additional favourable factors. Secondly, the growth of stores was facilitated by the establishment in certain districts of co-operative wholesale societies. Upto 1939, such societies were quite unknown. Beginning with the establishment of two such societies in 1939, their number increased. Another line of development in that province has been the growth in the number of Workmen's Stores. Even previously, some textile and other mills established stores for their own workmen. They were organised under the control of the employers and with the financial and other assistance received from them. The most notable of such stores is that organised by the Buckingham and Carnatic Mills in 1922 for supplying the essential requirements of the workers. The goods are sold at a low price, sometimes lower than that prevailing in the market, "often 25 p.c. less." But they are not truly workers' stores in so far as the entire management is in the hands of the mill authorities who are not even ready to grant the workers a share in management, possibly because they do not want to relax their control but mainly because it will open the door for outside interference who dominate so much over the labour organisations in this country. Whatever that may be, and although the possible danger of their degenerating into truck shops cannot be denied, yet so far, on the whole, they have been serviceable to workers. Since the commencement of hostilities, the Department of Co-operation in Madras has organised a number of co-operative stores for the mill workers in the Coimbatore, Madura and Tinnevely districts. The employers have been very much sympathetic and helpful to these stores. Thus the Madura Mills Company "has not only placed a very spacious building at the service of the society for a nominal rent of Re. 1/- per month but also granted loans to the tune of Rs. 80,000 at 4 p.c. interest, and what is more, it has given subsidies to the extent of Rs. 1 lakh, the principal object of which is to enable the society to sell provisions at less than cost price, in fact at pre-war prices. The society did not suffer any loss at first, because of favourable purchases made prior to the rise in prices. The members even got a rebate of one anna per rupee of purchases. But the loss

began from August 1941 and the Company had to make good the loss by a subsidy of Rs. 50,000." (*Indian Co-operative Review*. April-June, 1942, article by K. C. Ramakrishnan.) A fourth line of development in Madras has been visible in the federation of all the stores in a district into a wholesale society with a view to facilitating the purchase of goods, the two most outstanding examples of this being the Madura-Ramnad C. W. S. and the Coimbatore Central Co-operative Stores, but the loyalty of the members is greater in the case of the Coimbatore Stores possibly because "the board of directors of the Central Stores is more representative of the employers. By 1944-45 their number increased to 21, with 8764 primary stores as members. These wholesale stores have not only been linked up with the distributory system of the controlled articles but also have been recognised as "bulk importers" from Central and Northern India and have expanded their spheres of dealing even to non-members. But the sources of production are hardly co-operative and supplies are obtained from following sources: 62 p.c. from Government Civil Supplies agencies, 21 p.c. from production centres, 10 p.c. from private traders and 7 p.c. from other sources including less than 1 p.c. from co-operative sources. Finally, a new line of development that has crept in is concerned with the granting of credit facilities. The objection from the standpoint of co-operative principle against credit and its emergence in practical field even in England has already been noted. But the recent developments in the store movement in Madras also has not been free from this practice. Thus the central banks have been advised to extend credit facilities not only to store societies and the wholesale societies but also to members of rural credit societies to get their supplies from the stores on credit by the use of specially devised non-negotiable cheques. The store societies themselves have been permitted to sell goods on credit upto a cautious limit defined by the Department. It must however not be forgotten that these developments are confined to Madras only and have not affected or improved the situation in other parts. It remains to be seen how far these developments are naturalised in Madras in post-war years.

The most notable success attained by co-operative store

in Madras, and also in the whole of India is that attained by the Triplicane Urban Co-operative Society, which, judged by the Indian standards of the movement, may be spoken of as the Rochdale of India, started in 1904 by a group of fourteen men, on a humble footing, and making slow progress in initial stages. The society registered an advance even before the outbreak of the first world war. But the greatest expansion came in the years following the war, particularly during 1924-30. The progress was for the time arrested by the depression, but again started since 1938. On the 1st of December 1941, the number of members was 6724 (about 6000 during 1924-30 and 5570 in 1936). The paid-up share capital which exceeded a lakh in the years 1924-30, declined to Rs. 81,312 in 1938, but in spite of withdrawals permitted by the bye-laws, the paid-up share capitals went up once more to Rs. 91,771 in 1941. At the latter date the Society had a Reserve Fund of Rs. 1,08,250 and a Common Good Fund of Rs. 37,587. The Society deals in a variety of goods, mainly foodstuffs. It has a big depot in Nellore district for the purchase of paddy from the producers which it holds in stock and converts into rice by milling or by handpounding. It manufactures the gingelly oil and has to a great extent solved the problem of good supply of the same in the areas served. It also makes soap-nut powder on a small scale; so also, coffee is roasted and ground. It sells cocoanut oil produced by Messrs. Tatas at Cochin. Among other lines of goods handled, mention may be made of coffee, tea, other Indian beverages, sugar, almonds, cashewnuts, spices and condiments of several kinds, biscuits and sweets, toilet articles and a few drugs, charcoal, cattlefood, etc. The latest venture is the supply of piecegoods, particularly the handwoven products of several weavers' cooperative societies in the presidency.

Since the outbreak of the war, a greater degree of co-operation between the Triplicane society and the Madras Government, not in the matter of control but in the matter of expansion of its activities with a view to render assistance to the public, not only against the worst features of capitalistic commerce but at times when many private shops were closed owing to emergency, has been a remarkable feature. The Government assistance has in the main assumed two forms—to

permit the society to stock certain essential articles of consumption in special godowns, and to have a number of emergency shops opened in all parts of the city of Madras. Sales were thrown open to non-members, and articles consumed by the poor were also supplied.

Conclusion on Consumers' Co-operation.

The worst features of capitalistic retailing have never expressed themselves in so naked a manner as they did since the commencement of the second great war and the need for 'consumers' co-operation was never felt so intensively as it was at this time. Madras has proved more progressive in this matter than any other province. Thus the Registrar of Co-operative Societies in that province remarked that "if profiteering had continued the number and business of co-operative stores would have increased by leaps and bounds." The enlightened attitude of the government in that province has been of considerable help. The picture in other parts is just the reverse. Particularly in Bengal, where there is no co-operative store movement worth mentioning, with the increase in the fury of capitalistic commerce and the peculiar attitude of the government, the consumers have simply succumbed. It is after all a question of taking people into confidence. But the great gap that separated the consumers from those in power has always stood in the way and with the increase in profiteering, the helplessness of the people has simply increased. The only lesson left by this situation is that self-help is the best help and that for the future co-operative retailing, at least in supplies vital,—including their production, whenever possible, but at least purchase and store through sister organisations,—ought to have a good prospect in this country. If they can assume huge proportions, controlling not only price, but production as well, thereby having a predominant influence on the market, a great number of the ills of the present distributive machinery may be rectified.

Retail Trade Associations.

In capitalistic retail trade, tendency in recent years is towards the formation of Associations, which is a

new form of monopolistic organisation. During the last century, free trade was assumed to be the underlying feature of industrial organisation; but the course of business shows that the assumption was not correct, and quasi-monopolistic organisation underlies all business structures in all parts of the world. Even when quasi-monopolistic organisation came to be accepted as a normal feature of industrial organisation, people were cocksure that monopoly would never influence trade. In the words of Hermann Levy, who in his investigation on *Retail Trade Association in Britain* writes, "Just as it was supposed formerly that 'free trade' would make industrial combination impossible in this country, so nowadays the argument is frequently heard that the great multiplicity of trading outlets will never allow quasi-monopolistic retail trade organisations to flourish for any length of time. Yet Karze's in this country developed in spite of free trade and retail trade associations with the un concealed aim of restricting competition are to be found in every corner of trade activity in spite of the large numbers of single traders. But, again, similarly to industrial combinations in former days, retail trade associations have been fortunate to remain in the background of publicity." In this country in view of the fact that retail trade in most parts of the country is still in very old form of organisation, this new tendency towards combination is not very extensive. In some areas, as in Ahmedabad, the organisation very much resembles the primitive guild system. But in cities like Bombay and Calcutta where retail trade has sufficiently developed and can compare very favourably with the retail trade of any big city in the West, the recent tendencies at combination are not altogether absent. Some reference to this aspect has been made in connection with our discussion on combinations in commercial organisations in India in an earlier chapter.

CHAPTER VIII.

ORGANISATION OF FOREIGN TRADE.

Introduction.

It is too well-known a fact to need mention that exports of our country constitute imports of another country. We have considered, in brief, in Chapter VI, what the circumstances are under which a country imports goods produced in another country, in other words, the circumstances under which the producing country exports. There it was emphasized that goods are imported by a country, not because of its inability to produce them, nor because of cost advantages, but because it must. At least this is true for this country and also for smaller and dependent economies. Theoretical economists have all through been advocating the case for a free flow of international trade. Thus Staley writes, "A policy that restrains modern man from using the knowledge he has acquired, that restrains him from using resources in ways that have become essential to his present modes of existence in some parts of the world, builds up pressures for an explosion. Economic walls at national boundaries, far from preventing conflicts, themselves create a greatly materialistic basis for future wars. One of the first principles for those interested in economic progress and political peace must be: Lessen the economic significance of national boundaries." Or the *Report on World Trade*, issued by the British National Committee of the International Chamber of Commerce believes that "the most effective instrument of securing the economical distribution of production is a world market to which all have access without favour or discrimination; and in which rules a world price, locally modified by transport charges and as little as possible by tariff." These are bright pictures unsupported by reality, and the realistic study shows that the world market is being exploited by the big commercial nations for their personal benefit, even to the detriment of other countries, as

will be seen in connection with our discussion of restrictions on foreign trade and their consequences on India.

Export Agencies: Agricultural Products.

It is this item of discussion that is of major interest for us in so far as we are one of the most important countries exporting agricultural products to the world market. It is one of the grievances of the Indian trading community that the share of the Indians in their foreign trade is a negligible proportion. According to an estimate presented by the Indian Chamber of Commerce, Calcutta, in their representation before the *Central Banking Enquiry Committee*, the share of Indians in this trade is less than 15 p.c. of the total. This means not merely a loss by Indians in the matter of controlling their own foreign trade, but also a loss on account of commission, brokerage, insurance charges, etc., which constitute so very important items in her balance of payments and therefore a continuous drain on her resources. There is hardly any reason to expect that the situation has improved since the above representation was made; on the contrary, it has definitely deteriorated owing to the increase in the outflow of goods from India which has given a greater scope to these agencies to earn a lot. It should not, however, be taken that this exclusion of Indians from handling their own foreign trade is due to any inefficiency on the part of Indian merchants; just the reverse of it and in spite of so many difficulties it is really wonderful that they have, at least to some extent, however negligible, forced themselves in. The main reason for this disability is the peculiar attitude of exchange banks towards Indian concerns and the facilities that they grant to their own men, a fact which will be discussed in a subsequent chapter on financing of foreign trade.

Roughly speaking, the export trade of India, is in the hands of export houses working in the port towns, and sometimes having their branches in the upcountry centres. The details of their working differ slightly from commodity to commodity and may conveniently be studied for one or two of them. Let us take the case of the export of rice from India. These exports are of two types, either to the neighbouring out-

side markets or to distant markets. When rice is sent to, say, Ceylon or Mauritius, the exporting firms send goods in many cases to their own selling agents in the foreign markets. Occasionally, however, large buyers maintain their own agents in important producing centres or their representatives may pay periodical visits to the supplying markets to inspect the quality of the produce and make direct purchases. The machinery is however a bit complicated in case of long distance exports. A large proportion of the sales in distant overseas markets are made on the basis of a sample annually prepared by the London Rice Brokers' Association and are based on the average quality of the preceding season's shipments. The contract form of the Calcutta Rice Merchants' Association, which is more or less typical, includes description of rice to be delivered, quantity, price, date and port of shipment, terms of payment and delivery and provisions for the settlement of disputes. 95 p.c. of the bill or invoice value of the goods is advanced and earnest money may also be demanded from the buyer if the party is unknown or its status is in doubt. Generally however this condition is set aside as the parties are thoroughly well-known to each other. Exporters' selling contracts for Bengal rice shipped to Europe are almost invariably made on the contract of the London Rice Brokers' Association. Such sales are made with full guarantee and on ex-ship terms, the contract being signed in London by the representatives of the sellers living there and the buyers. The Bombay Rice Merchants' Association's contract is based on c. i. f. terms or godown delivery at Bombay at the discretion of the seller. Strictly speaking this contract is only for shipment and delivery rather than for futures transactions. It is the duty of the Association to look after the satisfactory fulfilment of the contract.

The export transaction through London has often worked against the interest of Indian rice. The trade of Europe in Indian rice being a small one, the London brokers have not paid much heed to Indian shippers, with an ultimate motive of not antagonising their clients of Burma or Siam rice who constitute a huge proportion of their trade. This has often been resented by shippers in India who have tried to establish direct relations with the buyers outside the United Kingdom.

Since 1936 and 1937, till the outbreak of the war, a certain proportion of the sales to European countries has been effected with Hamburg arbitration, and to North America with New York arbitration, and also with the West Indies direct.

The export trade in wheat also was practically monopolised by about half a dozen international grain merchants whose operations in India were controlled from Europe, usually in London. Most of these concerns had widespread buying organisations in up-country, consisting of a number of agencies and sub-agencies staffed with exporters' own personnel. This method was very common not only in the export of wheat but of barley, grain, oilseed, etc. An alternative method of purchase in the interior was through guarantee brokers working on the lines of commission agents. With the decline in wheat trade since the thirties a greater part of the inland organisations of international grain merchants was withdrawn, being regarded as uneconomic, and the guarantee brokers have come to occupy a more important role than previously. These purchases are made on port-pass contracts, which now account for half to three-fourth of the total quantities of wheat handled by shippers. This contract implies the acceptance by the seller of the buyers' weights and analysis in respect of goods railed by him to the shipper at the port of loading, in consideration of which he may have already received an advance of anything from 80 to 90 p.c. of the value of the goods sent either from the shipper's agency upcountry or from the port headquarters of the firm. The balance is adjusted after the goods have been accepted, weighed and analysed. The main conditions of a typical port pass contract are concerned with quantity of wheat purchased, quality, source of origin, crop year; type of packing and basis of admixture. The contract is non-mutual. For, if the goods contain more than the stated free tolerance, the buyer may either accept the goods with allowances in accordance with the buyer's scale of allowances for excess refraction in force from time to time, or reclean wheat at seller's expense, or accept the goods with an extra allowance to be fixed by buyer over and above the allowance according to the scale, or reject the goods claiming and recovering from the seller any loss. But if the goods contain less refraction.

than that allowed, no prominence is given to that. Another method of purchase by these exporting merchants is known as "agency pass." In this, goods are analysed, approved, weighed over and final payment effected on the spot by the exporter's local agency. In a few cases, wheat used also to be bought on "station pass" terms, which meant that the seller gave delivery at the Railway station and the goods were inspected and passed finally at that point. These export merchants then arrange for the export of wheat and similar other grains.

As in the case of wheat and other agricultural products, so also in the case of oilseeds, the export trade of India is mostly in the hands of firms of non-Indian origin, which have got their buying organisations in the inland centres. Among these firms, mention may be made of Ralli Bros., Volkart Bros., and Sassoons. In comparison with the quantity of seeds handled by them, the share of Indian export houses is almost negligible. The transaction between shippers in India and crushers in England and Europe is rarely direct, there being a long train of intermediaries between the two, particularly so in England where the banks are not so very lenient as to the granting of facilities to their customers, and the crushers, who need large sums of money to keep the mills provided with sufficient supply of oilseeds, have often to take recourse to the brokers.

Indian oilseeds are sold in Europe and Britain on the basis of the terms contained in the contracts of the Incorporated Oilseed Association, London. The contracts of the Association are very many, each being applicable to different types of oilseed, and there being in all 48 or 50 different contract forms. These contracts are based not on C. I. F. basis, but on "sound delivered" terms, the shipper being responsible for all risks upto the destination. The result of this has been that the contracts, containing as they do all sorts of clauses about risks, have become extremely complex. The most disquieting feature of these contracts is that they contain terms which are sometimes not quite in the interest of Indian shippers of oilseeds. Their complexity and intricacy and consequent lack of understanding have often involved Indian shippers in loss.

Or take the case of the export of sugar. Here the shipment is a monopoly of two concerns. It is well-known that under the International Sugar Agreement of 1937, India was

debarred from seaborne exports to places other than Burma. Under this agreement, which was in force till the other day, India was able to export sugar by sea to Burma and Ceylon and by land to Afghanistan, Central Asia, Turkistan, Tibet, Nepal, Sikkim and Bhutan. The procedure is as follows: Sugar is purchased by the exporters from the selling agents, although the goods are despatched direct from the mill siding to Rangoon *via* Howrah and if they are purchased on condition of shipment by flats, *via* Jagannath Ghat and bills of lading are sent direct by the mills to the exporters. The shipment to Burma is effected in case of Railway by M/s. Cox and Kings, Ltd., and in case of flats through M/s. Kilburn & Co. Over and above the price of sugar, the exporter has to pay 5 annas per md. to the selling agents for meeting various charges. When the goods arrive at Rangoon, the exporter has to pay Rs. 2/-per cwt. as excise duty and Re. 1/-to obtain customs certificate showing that the goods have paid duty in Burma. The exporter then obtains refund of excise duty from the mills on production of the said certificate. Most of the Rangoon merchants prefer to purchase sugar on condition that the exporters deduct the Burma excise duty from the sale bills, thereby foregoing the botheration. Various defects in the export procedure were brought to the notice of the Tariff Board on Sugar Industry (1938). It was pointed out that the difficulty with regard to excise and other matters was a severe handicap. As regards the refund of excise duty by the mills, it was pointed out that often four months elapse before the payment is received. But a greater complaint about excise duty was that the exporters could not get the refund unless they consigned sugar through M/s. Cox & Kings, Ltd., or M/s. Kilburn & Co. The notice of the Board was also drawn to the fact that on the arrival of goods at Howrah, the shipping agents take delivery and ship them by steamers; exporters are given no opportunity of examining the goods and they do not know the conditions of sugar before its despatch. The exporters cannot claim damages, which might have occurred during transit either from railway authorities or from steamer company. Nor do the exporters know when and by what steamer, sugar is shipped.

The purchase and sale of agricultural products in inter-

national market are effected either by oral agreements, through brokers, on the basis of samples, or by auction or through produce exchanges. In case of oral agreements on the basis of samples, the transactions are recorded by both the parties to the transaction by making appropriate entries in their purchase and sales books and may or may not be confirmed by letter. These entries which are not signed show such particulars as the date of transaction, quality, quantity, price and the name of the broker. If the goods are to be consigned to any destination outside the centre in which the transaction has taken place, the date of despatch and the place of delivery are also recorded. Business by oral agreement is governed by customs prevailing in each particular trade, and in many cases standard forms of contract are in use. In the preparation of sample from agricultural products, difficulties, however, are not rare, as is the case with the preparation of the "fair average quality" sample of Indian rice in London. This sample is prepared annually by the London Rice Brokers' Association and is based on the average quality of the preceding season's shipments. It is argued on behalf of the exporters that the succeeding crops may be a very good one in which case shippers would be consigning goods superior to the standard but would receive no premium. But if the crops turn out to be inferior, the shippers would be penalised. In other products, however, the condition is not as bad as that mentioned above. Whatever that may be, sales by oral agreement are based on sample. If the shipment has already arrived, the bulk may be inspected in some trades; in other cases a sample will be remitted to the intending customer. The warehouse accepts the responsibility for the sample being representative of the bulk. When sales are made against supplies that have not arrived, the trade descriptions denoting the trade are usually used as the basis of transactions.

Another method of sale dating back to the 14th century and subsequently perfected by the Dutch is the sale by auction. Products of a perishable character, and those which cannot conveniently be standardised and graded are generally sold by auction. Such products need be inspected by the intending customers for the determination of price. Such auction sales are to be found in London for tea, coffee and wool; in Amster-

dam and Rotterdam for rubber, tea, coffee, tin and spices and in New York in hides and furs. The increasing importance of international auctions has resulted in the development of local auctions in rubber at Singapore, in tea at Colombo and in other things at Dutch East Indies and elsewhere. In the aforesaid cases, auction sales take place in products derived from several sources. In recent years, auction method of sale is being resorted to on a large scale by individual concern or a group for the disposal of their products, though these methods are not so very common as that in products derived from several sources.

A more developed method of purchase and sale in agricultural products in international markets is through the mechanism of produce exchange, which needs a little elaborate study. The goods dealt in are those which are classified into well-defined grades, universally known, and these change hands on the basis of standard contracts. The daily prices of various commodities dealt in are being determined according to market conditions, and prices so determined may be taken as world prices. The local produce exchanges of different countries have connections with the international produce exchanges and are influenced by price fluctuations in the latter. The working of produce exchanges gives an idea as to how the prices of goods, dealt in in international trade are determined. It presents a remarkable realistic approach to price determination, as distinguished from the mere theoretical, static or dynamic, approach. It is well-known that the commodities dealt in are few, easily gradable, and universally recognised. Transactions take place through dealers, who, by their anticipations of future events and, operation accordingly, keep the market position more or less balanced. A study of the supply side is all the more interesting. The commodities dealt in may exist in another part of the globe; most often it does not exist. The seasonal outputs actually fluctuate; but the dealers in produce exchanges need not bother about them. Many of them may be interested not in goods, but in differences and the transaction is closed as soon as difference is received. This should not be taken to mean that there is no genuine transaction; there are, and possibly many. But many again are merely speculative and yet their role in the determination of prices is

by no means negligible. Exchange transactions cover two different types of dealings—spot and future. In spot dealings an agreed quality of a commodity is to be delivered immediately or at an agreed future date. The exchanges do not bother much over such transactions and after they have provided the central meeting place and laid down rules for members, their function is over. By far the more important type of transactions in produce exchanges are those concerned with futures contracts. As already said, dealers are not interested in commodity itself, nor would they like to receive it at the future date when the contract matures, so that by the difference they may gain or lose. It is this type of transaction that characterises the working of produce exchanges and determines prices of goods deliverable at some future date. Naturally the goods are those whose prices are liable to wide fluctuation with slightest change. For, if the prices are stable, no speculation can go on. Therefore, these produce exchanges are the best illustration of a free market, market where there is no control either as to price, or production or supply nor is there any monopoly in the goods. The market must be free, liable to fluctuation by the slightest ebb and flow. But even then the mere forces of supply and demand do not determine price; in both matters, there is scope for artificiality, a non-existent demand and a non-existent supply, which are mere creations by the operations of the dealer with a view to pocket the differences in prices. Free markets are less free than they are supposed to be.

Two recent changes in the export practice of our products may be noted here, before we bring the discussion on export agencies in agricultural products to a close. In the first place, Calcutta will henceforth be the world's tea centre instead of London. We have already noted that tea was sold by auction in London. Henceforth it will be done in Calcutta. This will not only mean greater revenue to the state derived from income-tax but also is expected to result in greater volume of sale when auctions are in full swing. The brokerage which used to go to London so far will also be retained in this country. Besides, the new arrangement will help the restoration of private trading in tea, in place of the bulk purchase contract which was so far arranged by the Government of India

on behalf of the British Government. Secondly, in place of granting export licences, a practice which was prevalent so far, the government are introducing the Tender System for exports. The drawbacks of the existing system were that the export licences were granted to established or approved shippers, that the new entrants were barred from participating in export trade, and that the existing shippers reaped undue profits by taking advantage of the big gap existing between internal and external prices of some export commodities. Thus according to the Indian Trade Journal, the price of groundnut oil in Madras towards the end of March, 1947, was Rs. 305 per candy of 500 lbs.; in London the price for the same in April came to about Rs. 655/-. The introduction of state trading would have brought this huge profit to the state but would have destroyed private trade. Hence a middle course has been adopted by the introduction of tender system which will apply in case of following commodities: (1) Non-essential vegetable oils and oil seeds, *i.e.*, groundnut kernel, groundnut oil, linseed, linseed oil and castor seed; (2) crushed bones and bone grist, and (3) soap. If this system proves successful, it should be extended to other commodities of export as well.

Export Agencies—Manufactured Goods.

Export agencies in manufactured goods do not interest us much in view of the fact that manufactured products constitute a minor proportion of our total exports. But, for the sake of completeness of our study we must mention the organisation and functioning of export agencies in advanced industrial countries. Although they are of limited interest to us at present, yet with the development of industrialism in this country, some or all of them will be of interest to us. As in other fields, the function of export being rather technical and complicated, specialisation has been no less essential in this field than in others. Accordingly, a number of agencies with varying organisations and working on different terms according to the nature of the services rendered, have come into existence. The work involved includes export proper, either direct to the importer, or through the intermediaries operating on behalf of

the country of import, the export being a sale on cash or credit terms, or on consignment, or through the sales organisation maintained by the manufacturer in the country of import, Banking facilities, shipping and insurance and market research, propaganda and promotion of sale. Of these, this section is concerned with export proper.

In export trade, two types of direct trading are quite well-known—direct trading with importers abroad, and direct trading through manufacturers' own organisation abroad. In both the cases, the manufacturing concern needs maintain an elaborate organisation for the purpose. Besides, there are various difficulties which may be obviated to a great extent by shipping goods through specialised agencies. Take the case of direct trading with importers. The imports of a single concern, however large, cannot compare favourably as regards the volume with imports through specialised agencies who would be handling them for a group, and thereby the latter can obtain economies in shipping and insurance charges which are by no means inconsiderable, but which may not be enjoyed by the exporter and importer in case of direct trading. True, the increased payment of freight and insurance charges may be covered by the importer in the prices, provided he is in a monopolistic or semi-monopolistic position; but under competition, it may either reduce his profit or impair his competitive position in the market. But a greater difficulty crops up in matters of credit risk. Before opening transaction with an overseas firm, the manufacturer must be absolutely sure in the credit-worthiness of the concern, in its integrity and efficient organisation in matters of pushing sales. But when the services of an export agent guaranteeing payment are utilised, this sort of risk may be eliminated. These agents will also render services in matters of converting prospective customers into regular ones and some of them may go so far in their working that the manufacturer can altogether or to a great extent eliminate the necessity of maintaining a propaganda service for the purpose, but in one type of export commodities direct trading is a necessity, I mean, in case of goods, particularly luxury ones, which are exported to cater for the varying requirements and tastes of the customers in the country of import. Thus it will be found that big departmental stores,

e.g., the British stores working in overseas markets, maintain a direct purchase service manned by experts who study not only the requirements and tastes of the customers but also the varied sources from which goods may be brought in at lowest costs and prices, and strive, in case of newly manufactured goods, to bring them into fashion. Leaving aside this case, direct trading with importer has been found less convenient and less profitable and is therefore not often resorted to in export trade.

Exports through the sales organisations of the manufacturing concern maintained in the country of import are less inconvenient but at the same time less profitable, as has been found by experience. They are less inconvenient in so far as the aforesaid risks are eliminated to a great extent; but they are less profitable in so far as the goods sold by them are not so large, except in exceptional circumstances, as to warrant the necessity of the maintenance of an elaborate sales service, and the possibility of making sufficient profit. Experience has shown that when in the first few years, sufficient profits are not forthcoming, the activities of the organisation are often supplemented by such activities as the import of goods from non-competitive lines for dealers inland as also export of raw materials and finished goods to their home country. These supplementary activities have enabled them to work with sufficient profits; but as a sales organisation, pure and simple, they are a failure.

Among the specialised agencies for the purpose of exporting manufactured goods, mention may be made of Export Commission Houses, Export Merchants and Export Agents. A considerable volume of export is handled by the first type of specialised agency whose position is essentially that of representatives of buyers overseas rather than sellers at home. It is a peculiar feature of these commission houses that they do not carry any stock on their own account; their only function is to supply orders from their overseas customers, for which they receive a commission on the value of goods purchased and shipped, the commission varying according to the nature of goods and services rendered. The powers of these commission houses vary according as the indent is open or closed. These indents sent to commission agents represent not order for goods, but order to purchase goods, sometimes from specified

concerns or to receive goods to whom order has already been sent. An open indent leaves the selection of goods to the agents while a closed indent gives full particulars of exact goods required and probably mentions price, brand and name of the manufacturer. Frequently an indent from the importer is followed by a counter-offer owing to the fact that the price on the indent is not acceptable to the merchant. When the offer is finally accepted, the importer sends a confirmatory indent to the commission house. The commission house then proceeds to arrange the purchase or to take delivery from a manufacturer specified in the indent and exports them to the proper destination.

Unlike the export commission houses, export merchants work on their own account and are responsible for their own profits and losses. They are not the manufacturers but purchase goods from them and sell them in the world market through their own selling organisations. Thus their function begins with the purchase and financing of goods, pass through the intervening stage of making provision for warehousing, and ends with their sale. Their function also includes market research and sales promotion. For the greater the volume of sale, the greater the distribution of distributing costs, and the greater the profits of the concern. It is the interest of the export merchants to purchase at a low price and to sell at a high one, the difference constituting their profit. Orders are placed directly with them, though, of course, they may contain details about goods. Accordingly, goods are arranged, packed and shipped by the exporting merchants. They do not charge a separate item as commission, for, the various cost items are included in the price quotation.

Certain recent tendencies in the functioning of British export merchants have been noted by MacEwan in his *Overseas Trade and Export Practice*. He writes that in recent years, great changes have come about in the activities of large merchant organisations. Owing to the highly competitive character of import business in manufactured goods and, also other factors, some of these merchants have gone into different and more specialised avenues of activity. They have turned from trading exclusively in general merchandise and applied their

energies, influence and capital to the marketing of products whose smaller importing firms overseas would be incapable of handling them. Engineering plant and equipment, building materials and other products, which require technical salesmen and specialised knowledge to deal with effectively, have had their particular attention. It has entailed the employment of technical staff and calls for a type of selling organisation differing considerably from that provided by ordinary importing merchants. These merchants are most often helped by the manufacturers in rendering these technical services to the importers. But even then it must be borne in mind that the manufacturer, though helping the export merchants in the sales promotions, are by no means responsible for the profits and losses of the latter.

A third variety of specialised agencies is known as export agents, who, unlike export commission houses, are working on behalf of the manufacturer, their principal function being to popularise the goods produced by the latter in the overseas markets. In case of smaller producers, however, a separate agent is too costly. Therefore, a sort of travelling agents have come into existence who work for different concerns at one and the same time. The selection of a travelling agent should be made with great care. Because, if he already be dealing in a competitive line, it is no use appointing him, for, he cannot do justice to two producers of rival commodities. This caution is equally essential for any other export agents as well, who may be working for other manufacturers in the same line. It is an advantage of the travelling agent that he can keep himself abreast of the developments in the overseas market and communicate them to his principal. The function of established export agents is simply to obtain orders, and, having secured them, to arrange the shipment through commission houses at home or through export merchants or packing and forwarding agents, the last named being those specialised in the specified functions.

A new type of selling organisation for the pushing of sales in overseas markets has come into existence in Germany, and to a slight extent, in U. S. A. Group action is very much suited to the German genius as is evidenced by the formation

of Kartells in the field of production. The field of distribution is also not immune from the peculiar influence of German genius. MacEwan mentions the following types of group-selling organisations devised so far:

“(1) A group of manufacturers sharing the cost of maintaining an exclusive resident agent in an overseas market, who devoted all his time to marketing the products of the group.

“(2) A marketing company formed by a group of manufacturers to operate a particular overseas territory, the expense being shared between the members in agreed proportions.

“(3) An independent company with overseas branches which acts as the selling organisation for a limited number of manufacturers who contribute to the overhead expenses on a turnover basis and are charged individually with any costs incurred specially for their benefit.

“(4) An association of manufacturers in a particular industry, having a central sales organisation responsible for working overseas markets and dividing the orders received amongst the associated firms in agreed proportions.”

Doubt has often been expressed as to the efficacy of this method of selling on the ground that it submerges the individualism of different concerns into the group-selling organisation in matters of sale and therefore may not be liked by those countries which are imbued with a spirit of individualism. So far as small producers are concerned, it sometimes remains not a question of liking but of necessity and the conditions of world trade have changed so far that newer devices need be adopted for the capture of new markets and for the maintenance of footing in the old

We have already said that in matters of export of manufactured goods we are not much interested. The slight interest that we have concentrated round the export of piece-goods. Our interest in this respect is shown in the following Table from the *Review of Trade* 1940-41.

(In million yards.)

	Mill Production.			Exports.		
	1938-39	1939-40	1940-41	1938-39	1939-40	1940-41
Grey & Bleached Piecegoods:—						
Shirtings and Longcloth	1040.1	1011.6	969.0	12.4	11.4	30.4
Chadars	74.6	70.6	61.9	4.0	3.5	6.2
Dhuties	1454.8	1230.3	1101.4			
T. cloth, domestics and shirtings	183.3	173.2	181.2		0.1	
Drills & Jeans	135.2	122.3	187.8	1.0	1.6	10.0
Other sorts	449.1	478.3	664.1	61.4	76.8	133.1
Total	3337.1	3086.3	3165.4	78.8	93.4	179.7
Coloured Piecegoods	932.2	926.2	1104.1	98.2	128.0	210.4
Total piecegoods	4269.3	4012.5	4269.5	177.0	221.4	390.1

Other manufactured commodities in whose export India is interested are jute bags and cloth whose export quantity was shown as follows in the *Review of Trade 1940/41*:—

	1938-39	1939-40	1940-41
Bags (in millions)	598	1211	678
Cloth (in million yards)	1550	1561	1546

The need for a common selling organisation in the territories served by Indian piecegoods has been emphasized by the Tariff Board on cotton textiles. The Board considered that a better organisation of the export trade in piecegoods would be of considerable assistance to the mill industry in Bombay. In

1928 the Indian Trade Mission was appointed for carrying on a survey of some of the territories mentioned in the Tariff Board's Report. Among other things, the Mission recommended the appointment of Trade Commissioners at three places, of which two were appointed at Alexandria and Mombasa. The Tariff Board had recommended two further lines of action. In the first place it recommended that the industry should examine the feasibility of a combination of the mills interested in the export trade for the purpose of arranging such details as the manufacture of the lines required, the allocation of quantities among members and the prevention of imitation of marks and numbers. It was also recommended that in its own interests the industry should have its own representatives in the principal export markets, which being done, in the opinion of the Indian Trade Mission, an additional market for 80 to 90 million yards of cloth could be found only in the territories investigated by the Mission. Unfortunately, none of the recommendations found favour with the industry, the former on the ground of impracticability and the latter on that of expenditure for a sales organisation. Even a few years back, the *Bombay Textile Labour Enquiry Committee* made similar recommendations in support of the above ones, when they pointed out that "the evils of unregulated competition are so obvious that the need for some form of joint endeavour becomes imperative. The division of the market on the basis of the sources of supply, the allocation of production of specialised sorts to specific units or centres, the better organisation of export markets for the common benefit of the industry—these matters must receive earnest attention if unbridled competition is to be checked." The conditions of world trade have changed all the more in the last few years and if Indian piecegoods industry is to survive the scramble that would ensue in post-war world, it should give up all sorts of conservatism and combine in matters of production and distribution, and adjust its distributive organisation to the situation as it demands.

Apart from the need for joint action, it is essential that the Indian businessmen should be alive to the building up of sound reputation in foreign markets. It is this aspect which is most neglected. The Middle East Countries are our important

customers and even there our business reputation has reached a very low level, as was found by the members of a Trade Delegation which recently visited some of these countries. While the members of the Delegation found everywhere a keen demand for Indian goods, everywhere they met with complaint about the lack of integrity of Indian business. A few examples have been given: a firm of Turkish importers of Indian pepper had received a huge consignment of pepper mixed with crushed black stone; importers of cutpieces in Saudi Arabia where cloth was in great demand complained that a large number of bales included cloth which was torn and unusable owing to age; and a large consignment of shoes imported by business houses in Persia were found on examination to contain a disconcerting proportion of cardboard. Similar complaints have recently been received from America. The government was in part responsible for this state of affairs in so far as the export licences were given injudiciously and the Government representatives in overseas countries had made little effort to examine the bonafides of applicants for import licences. Even the Indian exporters are to be blamed for their "callous indifference" towards their customers in East African markets who complain about the discrepancy between the quality of samples and goods actually supplied, defective packing and finish and such other deficiencies. It should be realised in the first place that our export items are now more and more becoming manufactured products, and not raw materials, for which we will require foreign markets in future and secondly, with the approach of more normal times, competition is sure to ensue with western countries in Mid-East markets and if the Indian businessmen are not sufficiently alive to this fact, we are sure to lose the market which we have captured during war years at heavy cost. Already we are in danger of losing our export market in East Africa for groundnuts. Our markets in other products will also prove short-lived if sufficient care is not taken from now.

Technique of, and documents in, Foreign Trade.

When a new customer wants to import goods, it is usual for him to make an enquiry as to the quotation so that he can estimate whether under existing conditions of the market he

can profitably import a particular commodity. So far as the importing merchant is concerned, the price of the goods, unless they are a new line, is already determined and it is for him to see whether, within the price limit so determined, he can earn a profit after meeting all sorts of costs. In replying to this enquiry, practice has long been common in foreign trade to mention a few letters after the actual quotation in currency, the letters indicating certain recognised rights and duties of the buyers as well as the sellers, both being bound by certain international trade usages, supplemented by laws of the particular countries concerned. To take one example, before the rise of the sugar industry in India, we depended mainly on imported stuff. The import business was in the hands of firms with their head offices in principal ports who bought through their branches or agents abroad and sold to merchants on c. i. f. basis. These three letters indicate that costs, insurance charges and freight charges were paid by the importing firms, all these items being included by them in the price that they charged from the merchants. The merchants in their turn sold to dealers who took delivery at port after paying import duty and landing charges. The following letters or abbreviations are in use. Their significance is written against each.

(a) *Delivered docks*—Price includes charges of unloading and delivery to docks at the port of departure.

(b) *F. A. S.* (*Free alongside ship*)—delivery will be given to the side of the ship, but any charges for loading on to the ship being extra.

(c) *F. O. B.* (*Free on Board*)—Here the quotation includes the cost of loading on board the ship. The duty of the seller ends here. Of course, he will secure from the shipping company some form of receipt for the goods and to hand this over to the buyer.

(d) *C. & F.* (*Cost & Freight*)—The freight is paid by the seller who obtains the necessary bill of lading from the shipping company. Since the freight is paid by the seller, the quotation makes specific reference of the port of destination, for which the price is quoted.

(e) *C. I. F.* (*Cost, Insurance, Freight*)—all paid by seller.

(f) C. I. F. I. (Cost, Insurance, Freight, Interest)—The quotation includes interest on the value of the shipment.

(g) C. I. F. C. I. (Cost, Insurance, Freight, Commission, Interest)—The quotation includes agent's commission.

(h) C. I. F. E. (Cost, Insurance, Freight, Exchange)—The quotation covers risk of exchange fluctuations.

(i) Ex-Ship—In this case the seller will pay all expenses upto the time the goods arrive at the port of discharge but the buyer must bear the cost of taking delivery from the ship.

(j) Landed—The seller bears all expenses till the goods are landed at the port of destination.

(k) In Bond—The seller will deliver the goods in the customs or bonded warehouse at the port, but any charges for withdrawal therefrom and for import duty have to be borne by the buyer.

(l) Duty Paid—Here the quotation includes import duty, and sometimes even the warehousing charges.

(m) Franco, rendu or Free—Delivery in this case is given in the buyer's godown, all the costs upto that time having been included in the price quotation.

Documents—Bill of Lading.

The most important document used in export trade is the Bill of Lading (B/L), issued by the shipping company or their agents. The B/L is used in a set of two or three. The first clause in the B/L is the clause Paramount stating that the goods are being carried subject to the terms and conditions of the law, if any, on the subject in the particular country to which the ship belongs. Other clauses are concerned with the duty of the ship in certain unforeseen incidents, like refusal to permit entry at the port of destination, happen and also with the conditions of carriage, delivery, etc. The B/L is, so to speak, an acknowledgement by the shipping company or their agents for the receipt of goods in package. The company is simply responsible for the carriage of these goods as they are delivered. The B/L, no doubt, mentions the name of the goods declared to be inside the package; but the company does not hold itself responsible for their quality and quantity. Of

course, the deterioration of quality should not have resulted owing to the negligence of the company. When the company is working properly under the rules and usages, it only holds itself responsible for the number of packages, and not for goods therein.

The B/L is not simply an acknowledgement; it is also a contract for the carriage of goods on payment of a certain freight specified therein. The B/L may be Freight Prepaid or Freight Collect. In the latter case, the shipping company has a lien on goods for any unpaid freight, and it will not part with them unless and until the freight is paid. The company has also a lien on goods and right to retain them in case of general average or salvage claim; for if a ship or cargo is exposed to the danger of damage or destruction for averting which some part of the cargo or the ship suffers damage or is destroyed, a contribution is claimed from all the shippers.

When the contract between the exporter and the importer is for delivered dock or F. A. S., the duty of the former is simple enough. But complications arise in any other form of contract beginning from F. O. B. onwards as shown above. For, in the latter case the exporter must see that the goods are placed on a particular boat specified by foreign buyer. If this is not done and goods are carried in a different boat and reach the port of destination earlier or later, the importer has the legal right to refuse acceptance and sue the seller for the non-arrival of goods and for any loss consequent thereupon. Even when the contract is for F. A. S. delivery, the exporter must be careful to see that he does not violate any specified or implied term of the contract. Thus if the contract is for the delivery of goods alongside a particular ship, he must be careful to see that they are so delivered. The same is true as to the specific mention as regards the date of export. If none of these are mentioned, even then the seller has certain duties, though implied, which are governed by the trade usages, which if not complied with, the seller may stand to lose.

When the goods have been properly despatched by a proper ship within proper date, the exporter sends one copy of the B/L to the importer by the first mail, to be followed by a second copy by the second mail, if possible, by an alternative

route. Sometimes a copy is sent in the ship's bag in order to remove the possibility of delay in its arrival and of incurring heavy demurrage charges. The exporter must make it a point to despatch the B/L and other documents properly so that they may reach the proper hands; for if they fall into wrong hands, the buyer may find that the goods have been taken away by somebody else, may be a rival competitor. The goods may have been shipped in the name of the consignee in the country of import or, his order, when he maintains office inland or in an upcountry centre. Sometimes, however, the goods are booked in the name of the consignor himself, particularly so when goods have not yet been sold. If in the meantime the exporter can negotiate a sale, he will endorse the B/L and send it to the buyer. Otherwise, his own agent in the country of import will receive goods on his behalf. Where a successful negotiation is effected, the law recognises the mercantile practice of effecting sale in this manner and the person or firm in whose favour the endorsement has been given will be entitled to receive goods from shipping company.

When there is no direct shipping link between the country of export and that of import, some difficulty arises, for the exporter has to arrange the carriage right through to the port of import and must therefore get a Trough or Transshipment B/L, thereby arranging for the subsequent carriage by the second vessel.

Goods exported from India are carried almost wholly by steamers, although large seagoing *dhow*s ply between the west coast of India and destination in the Persian Gulf, on the Arabian seaboard and even as far as the African continent. Goods exported may be shipped by one of the regular steamer services operating between Indian ports and foreign countries. When large quantities are concerned, vessels may be specially chartered in London by the exporter for this purpose. For obvious reasons, freight by chartered vessels is almost invariably lower than that by regular liner tonnage services. Chartering vessels for full cargoes is effected on the Baltic Exchange in London, freight being payable in U. K., generally London, after the goods have been discharged. Liner space is booked through freight brokers at the ports in India and the freight is payable at the port of loading.

Policy of Insurance.

Another very important document in trade is the insurance policy. The insurance is effected by the exporter or the importer with the insurer according to the terms of their contract. Thus, *e.g.*, in case of C. I. F. quotation, it is to be effected by the exporter whereas in case of F. O. B. quotation, it is the duty of the importer to take a policy. The premium is paid to the insurer according to the nature of the goods and risks involved in their export, the rate being determined by the company. The party concerned may take a separate policy for each shipment or cover a number of shipments under a floating policy, otherwise known as open cover, the latter being convenient for those who have to export or import from time to time. When various types of goods are exported, some trouble may arise in the taking of floating policy, because the rate for each commodity may be, and actually is, different from that of another, according to the perishableness, value and dangerousness of each good. For the sake of convenience therefore the insured pays an agreed "basic" rate, the balance due to or from the insurer being adjusted when the policy is completely used up.

Invoice.

This document is prepared by the exporter and is a *prima facie* evidence of the contract between the two parties in the transaction. The buyer cannot however check the correctness or otherwise of this document until the goods have been received. Upto that time, the invoice is accepted as being correct, any mistake as to goods or prices being rectified afterwards and adjusted by the exchange of credit and debit notes.

Certificates of origin, of weight, and of chemical analysis.

In case of many countries, permission to land the goods is refused, unless the buyer produces a certificate of origin. This is useful for two purposes. When the entry of goods from a particular country is banned, such a certificate is called for in order to make sure that the goods did not originate in the country so deprived. The same is true in case of preferential

tariff. In order to take the advantage of preference granted to the goods of a particular country, other countries may send goods to the latter country, to be re-shipped to the country granting preference, thereby evading the hardship inflicted and taking advantage of the preference. In order to make sure that the goods do not come from the country whose goods have been banned entry and that the preference is enjoyed by the goods of the country to which it has been granted, the certificate of origin is widely used, and has become a very important document in recent years in case of those countries like, England, France, etc., who maintain an imperial trade and have adopted a policy of mutual advantage in trade between different units of the Empire. The certificate as to the weight is important in case of those goods where the parties to the transaction have agreed to make and receive payment on the weight of the goods sent. Thus in case of goods which have a tendency to evaporate, it is better for the exporter to take one such certificate from the shipping company, so that, on its production, he may receive payment on the weight at the time of shipment, any loss in the way due to evaporation being shifted over to the shoulder of the importer. In determining the standard of certain articles in whose case the chemical composition of the articles transported counts most at the time of payment, one such certificate of chemical analysis is also attached. This is of importance in the export of metallic ores.

Consular Invoice.

This is another important document used in foreign trade and is required by the laws of many countries for supporting the other documents. Essentially this is a copy of the invoice prepared by the exporter on an official form. The country of import maintains a consul in the country of export, who then affixes a revenue stamp of his own country and appends his signature on it. This document facilitates the clearing of goods through the customs at their destination and serves as authentication of the particulars given.

Restrictions on Foreign Trade—Tariff.

As in other fields of economic theory, so in this field of

international trade also, the classical writers have all through advocated the free flow of international trade. But the practice has, at the same time, differed all through and restriction in some form or other has been an essential feature. The most common policy in this respect has been the imposition of tariff, specific, *advalorem* or mixed, on imports and/or exports. A study of the tariff of different countries is extremely important, in practice, not only for calculating whether it is profitable to export goods to a particular country but also for seeing whether by some alteration in standard packing or in the goods, the advantages of the lowest possible duty can be availed of. Sometimes changes are made in the rate of customs duty with a change in price in order to maintain the effectiveness of the former and it is essential that the trader must keep himself up-to-date about these changes. Specific duties being levied on weight, measurement, quantity or volume, it differs from commodity to commodity according to the nature of each. When it is levied on weight, it may vary according as the law defines the weight to be charged. It may be gross weight including all packings, net weight excluding all packings, the weight being that of the goods proper and intermediate weight in which case one cover is taken into weight, but not the outer packing. In case of number the rate of duty may be concerned with each article, a pair, a dozen, a gross or one hundred. So also in case of measurement. Whatever the nature of the duty imposed, it constitutes an obstruction to the free flow of trade. No less complicated is the structure of *advalorem* tariff. It may seem at first sight that the *advalorem* tariff is simpler than the specific one, in view of the fact that in the latter specific items are taken into consideration, whereas in case of the former, the duty is imposed on the value of goods imported. But the basis of value for the assessment of the duty is not the same in different countries. For, sometimes the wholesale value in the country of origin is taken as the basis whereas at others the value of the port of shipment and at still others value includes such item as insurance, freight, etc., the last variety being the characteristic of British Tariff. In U. S. A., the duty on certain imported goods is levied on the selling price, in which case the importer is directly affected, unless, of course, he

includes the duty in the price calculation beforehand. In some of the smaller states of South America, and some countries of Europe, Egypt, etc., "official values" are determined by a panel of Government officials and businessmen, the value so determined remaining unaltered notwithstanding the fluctuation in prices, and thereby ensuring more or less stable revenue.

Until recently the Indian import tariff has been over-cautious. Upto 1857, the year of the great political and military upheaval ever seen in India since the beginning of British rule, the object of the tariff seems not so much the revenue as the encouragement of imports, particularly from England in British vessels, discriminatory duties being imposed not only against non-British goods, but also against any goods, British or non-British, being carried in non-British vessels. Thus the year 1811 saw the introduction of preferential duties in India in favour of British goods, which took about three quarters of a century for other Dominions to accept in favour of Great Britain, the response from England coming after more than a hundred years. Thus although the idea of preferential treatment to the mother/dominating country is new, being associated with Joseph Chamberlain, the practice dates back to 1811 so far as India is concerned. The upheaval was followed by an increased demand for revenue on the part of the Government and all import duties were therefore raised in 1859 to 20 p.c. This resulted in the operation of the Smithian dictum that in matters financial two and two do not make four but may make one and was therefore immediately revised in downward direction, the preferential treatment to British goods having been abandoned, and the basis of valuation also having been revised. The process of reduction of import duties, "under pressure from the British Government inspired by the Manchester interest," started from 1864 and by 1882 all customs duties were abolished and India became a free-trade country in imitation of England and to the immense detriment of her own economic interest. Between 1882 and 1894 there was practically no import duty. But in 1894 owing to the financial stringency caused by the falling rupee, a 5 p.c. general *advalorem* import duty, with certain exceptions, was imposed. Between 1899-1904, certain countervailing duties

were imposed on bounty-fed sugar coming from some European countries, the effect being the diversion of imports from Europe to Java and Mauritius. In 1910, certain customs duties were raised in view of the approaching reduction and gradual extinction of the opium revenue.

Some important changes took place in the customs tariff of India during the war and post-war years. Thus the general *advalorem* duty was raised to $7\frac{1}{2}$ p.c. in 1916-17, excluding cotton piecegoods, they having been included in 1917-18; to 11 p.c. in 1921-22, including cotton piecegoods; and to 15 p.c. in 1922-23, cotton piecegoods remaining at 11 p.c. A duty of $2\frac{1}{2}$ p.c. on railway materials was levied in 1916-17, to be raised to 10 p.c. 1922-3. Increases in duty were also made in case of iron and steel, sugar, luxury goods like motor cars, cinema films, watches, silk piecegoods, etc., and new tax imposed on machinery and stores for cotton spinning and weaving at $2\frac{1}{2}$ p.c. in 1921-22, to be abolished later on. A high specific duty on matches was imposed in 1921-2 at 12 annas per gross boxes, instead of $7\frac{1}{2}$ p.c. *advalorem* duty, and was doubled in 1922-23. Evidently the tariff was by no means uniform. Because of the high duties and their uncertain tenure, they, instead of giving protection to industries, actually impeded their development. *The Taxation Enquiry Committee* characterised the tariff as it stood in 1924 as a revenue tariff in the main and pointed out that the haphazard charges had introduced difficulties in classifying goods and in their appraisement.

There were drastic changes during 1930-35 with a view to meet the deficit caused by the depression. *The Finance Act* of 1931, passed to meet the situation, led to an increase in duty in certain respects. Thus the duty on ale, beer, cider and other fermented liquors were increased by about 66 p.c. above the old level, and those on wines and spirits, excluding denatured spirit were raised by 30 to 40 p.c. Duties on all grades of sugar and sugar candy were raised by Re. 1-4-0 per cwt. The duty on silver was raised from 4 annas to 6 annas per ounce, and spices, betelnuts and cinema films were transferred from the general 15 p.c. *advalorem* rate to luxury rate at 30 p.c. Apart from these increases, certain surcharges were also levied. A surcharge of $2\frac{1}{2}$ p.c. was imposed on articles bearing 10 p.c. duty, 5 p.c. on articles bearing 15 p.c. or general rate of duty,

10 p.c. on articles bearing 30 p.c. and other important surcharges on certain goods. Thus a surcharge of 15 p.c. was levied on cigars, Re. 1/8/- per 1000 on cigarettes, 12 annas per lb. on unmanufactured tobacco, 9 pies per gallon on kerosene, 2 annas per gallon on motor spirit, 10 p.c. on motor cars and cycles, $2\frac{1}{2}$ p.c. on artificial silk yarn and thread, $7\frac{1}{2}$ p.c. on silk mixtures, Rs. 2 per ton on imported cement, and 5 p.c. on the basic duty of 15 p.c. on cotton piecegoods. The *Supplementary Finance Act* of 1931 (November) effected further increases of 6 pies per lb. on raw cotton, 10 p.c. on machinery, 10 p.c. on dyes, Rs. 7/4/- on brown sugar, 15 p.c. on artificial silk yarn. 40 p.c. on artificial silk piecegoods and electric bulbs and surcharge of $\frac{1}{4}$ of the existing rates on all customs imports including surcharges imposed by the preceding Finance Act and also new duties with certain exceptions. Since 1932 the tariff policy is influenced and shaped by the Ottawa decisions, which will be considered later in this discussion. The next important change came with the *Finance Act* of 1934 which changed the duty payable on cigarettes to 25 p.c. advalorem and in addition either Rs. 8/2/- per 1000 cigarettes or Rs. 3/4/- per lb. whichever is higher. It also increased the duty on unmanufactured tobacco to the standard rate of Rs. 3/4/- per lb., the Colonial Preference rate being Rs. 2/12/- per lb. It should however be emphasized that the above duties have been more of revenue than protectionist in character and it is peculiar that while the yield from customs in the case of other agricultural and raw material producing countries had declined since the depression, that in India had not been allowed to drop. (*of World Economic Survey* L. O. N. 1933-34. Pp. 226-30). Thus declared the Finance Member in his Budget speech for 1939-40 that "At the present moment, even over the revenue part of the field, customs duties in general are as high consistent with a maximum yield, while over the protective part, the return is rapidly declining." That should not however be taken to mean that this decline in the yield over the protective part is due to the largescale industrialisation of the country. This decline is due to the decline in imports which were practically halved by 1931-32 over the 1929-30 figures and continued almost at the same figure till about 1936-37 and slight increase was recorded in

subsequent years. "What with the small proportion and what with the low level of duties and the small degree of positiveness about them, the effect of the protective measures must be comparatively small."

Restriction is imposed not only on imports but also on exports which prohibits or restricts the outflow of certain commodities. In this matter also the policy of the East India Company favoured exports to Great Britain over exports to any other country, the policy being abandoned in 1848. When the administration was taken over by the Crown, export duties on a number of articles, like jute and tea, were abolished. In the sixties, owing to the budgetary difficulties, a heavy export duty on saltpetre was levied, with disastrous consequences. By 1874 however all export duties, except those on rice, lac and indigo, were abolished, and those on indigo and lac being abolished in 1880. Since then, upto 1916, the only export duty was that on rice. But in that year jute and tea were subjected to duty. In case of tea the export duty was fixed at Re. 1/8/-, but was abolished in 1927-28, and was succeeded by an increase in income-tax assessment on the profits from tea industry. The export duty on jute was fixed at Rs. 2/4/- per bale of 400 lbs. Manufactured jute was charged at the rate of Rs. 10/- per ton on sacking and Rs. 16/- per ton on hessian. The duties on jute were doubled in 1917-18. An export duty on hide and skin at 15 p.c., with a rebate of 10 p.c. for export to Empire Countries, was imposed in 1919 with a view to help the tanning industry in India and to encourage export to Empire Countries. The ground for the latter course was that the native industry would not be able to absorb the whole amount exported. But as none of these objects was realised, the duty was lowered to 5 p.c. and the rebate abolished in 1923. In 1930 the export duty on rice was reduced by 9 pies. The duty on raw hides was abolished in 1934 and that on skin in 1935, when it was found that the duty was exerting adverse effect on exports, particularly to Germany.

We have given above a brief account of the customs duties in India. So far as these duties are concerned, they have been mainly revenue in character. Whatever that may be, they represent a sort of restriction on the free flow of international trade. In recent years the more advanced countries have given

some thought to find out a more rational tariff structure which may be immune from the effect of price fluctuations. It is well-known that changes in prices affect in different manner the specific and *advalorem* duties; for, unlike *advalorem* duties, specific duties do not respond to the changes in price level. Opinions differ as to the efficacy of either method as such. Thus Dr. Gregory states that specific duty yields a better result, because *advalorem* duty increases the burden of the duty on the importer when price burden has increased and decreases the duty burden when price burden has decreased. Contradicting Dr. Gregory, U. Hicks argues that his discussion rests on the implied assumption that only the price of a particular commodity is changing, all other prices and money incomes remaining the same. According to him, "During changes in general price level, an unaltered schedule of *advalorem* duties adjusts itself automatically to the change in price levels so as to maintain the same relative degree of severity on taxpayer and to bring into the treasury the same amount of purchasing power. Specific duties, on the other hand, become more severe on the taxpayer during a period of falling price levels and less severe during a period of rising price levels. These are theoretical squabbles. The practical businessman knows that in case of *advalorem* duty, it being a proportionate part of the price, the proportion remains a constant factor under conditions of price fluctuation. When prices go up, the duty goes up proportionately; so it declines with price decline. In case of a specific duty, the duty remains stable and therefore represents less additional cost so far as consumers go under conditions of high prices. The specific duty has disadvantages when prices decline, since even then the duty remains a stable factor in price. At that time, the *advalorem* duty is in an advantageous position. This experience has induced some countries to experiment with mixed tariffs. A middle course was adopted by the French Government who, in their endeavour to maintain specific duties, established an administrative commission with power to multiply specific rates by "value co-efficients" corresponding to changes in price of particular group of commodities. In the present stage however the discussion of mixed tariff is only of theoretical interest in this country.

Quotas and Trade Agreements.

Another method of imposing restriction is to fix the maximum quantity of a particular commodity that may be imported from a particular country. This is often the result of agreement between two countries. The objectives may be either to secure a certain proportion of the home market to national products, or to conserve foreign exchange resources so that they may be more usefully utilised, or to protect against the uninterrupted flow of goods from countries with depreciated currencies or to foster import from the dominating country in case of Empire. So far as we are concerned, the last two objectives are of importance, and are expressed in the trade agreements with Japan and Britain. It is well known how under pressure of Japanese competition as a result of the depreciation of the yen the Indo-Japanese Trade Convention of 1904 was denounced by the Government of India. But the continuous depreciation of the yen increased the intensity of the crisis in cotton industry and was followed by an increase in import duty on non-British cotton products. However, after much bitterness and retaliation, an agreement was entered into as a result of which the import duties were determined and a system of quotas was fixed for the import of Japanese cloth into India and the export of raw cotton from India. Under this arrangement Japan was allowed to export to India in any cotton piecegoods year, *i.e.*, the year beginning on 1st April, 325 million yards of cloth provided she purchased one million cotton bales from India in any cotton year, *i.e.*, the year beginning on 1st January. This was basic quota. In any year Japan could send the maximum quantity of 400 million yards of cotton piecegoods. In this case, the basic allotment of 325 million yards was to be increased by $1\frac{1}{2}$ million yards for every ten thousand bales of raw cotton taken in excess over one million bales taken in any cotton year. The above quota was exclusive of re-exports. The cotton piecegoods that might be imported was sub-allotted as follows: 45 p.c. plain greys, 13 p.c. bordered greys, 8 p.c. bleached (white) goods, and 34 p.c. coloured (printed, dyed or woven).

The quota so prescribed did not work satisfactorily. It was argued by some people that the Agreement was entered

into under threat of not purchasing cotton from India and therefore Japan was in an advantageous bargaining position. Whether it was the result of threat or not, there can be no doubt that there were many loopholes in the quota system and they were availed of by Japanese as well as Indian merchants in Japan. Thus the cuttings of cloth pieces below the standard length were exported from Japan and Indian merchants developed a considerable trade in them. Since the customs duty levied on them was small, the merchants found their import advantageous. Another method of evading the agreement was the export of readymade goods. Under the new *Indo-Japanese Trade Agreement* of 1937, the annual basic import quota of Japanese piecegoods has been reduced from 325 million yards to 283 million yards while the export quota of Indian cotton has remained the same. In the same way, the maximum limit of imports of cotton piecegoods from Japan, which is conditional on that country's importing $1\frac{1}{2}$ million bales of raw cotton from India, has also been reduced from 400 to 358 million yards. This change however did not improve the position because the reduction was effected owing to the separation of Burma from India, all other defects remaining untouched.

Whether effective or not the fixation of quota with Japan was the result of that country's policy of trade expansion under the cover of currency depreciation. Altogether different circumstances led to the *Bombay-Lancashire Textile Agreement* of 1933 and the *Indo-British Trade Agreements* of 1935 and 1939. The agreements were aimed at fostering imports from England on the ground that "owing to lower costs and other factors operating in foreign countries, the industry required a higher level of protection against them than against the U. K." The Agreement of 1939 provided for certain quotas. The Agreement provided that the dutiable cotton fabrics would be subject to the basic rates of $17\frac{1}{2}$ p.c. on printed goods, 15 p.c. or 2 annas and $7\frac{1}{2}$ pies per lb., whichever is higher on grey goods and 15 p.c. on all others. If however in any year the U. K. imports do not exceed 350 million yards, the duties charged after the end of that year and until the end of the year in which such imports exceed 425 million yards are to be reduced still further by $2\frac{1}{2}$ p.c. with a proportionate

reduction in specific duty on grey goods. If in any year however the U. K. imports exceed 500 million yards, the rates of duty in the following year may be increased above the basic rates to such extent as may be deemed necessary to the purpose of restricting imports. Similar agreement was entered into between cotton exports from India to U. K. and cotton piece-goods imports from U. K. into India. The Agreement of 1939 was necessitated in view of the fact that the agreement of 1933, otherwise known as the *Mody-Lees Pact*, though based upon reduction of duty on British piecegoods and yarn in exchange for an undertaking on the part of Britain that Indian cotton would be popularised in Lancashire, made no definite provision as regards the latter. But even the agreement of 1939 was not sufficiently clearcut as to the exchange of goods; it was concerned with basic rates of duty and not with basic allotment of the quota.

Trade agreements are generally entered into for seeking advantages to the national economic interest. But the trade agreements entered into by the Government of India have not received the admiration of the Indian trading community. Let alone the politicians. But one thing is clear from an impartial viewpoint. It is this that the representative Indians have scarcely a say in the matter; and although the commercial bodies may be consulted in the matter, they have no influence on those who determine policy. But then the greatest handicap lies in the various commercial safeguards imposed on India which no independent country would tolerate. In spite of the repeated expression of disapproval of these safeguards by Indian commercial bodies throughout the country and of the nationalist section of the Indian Legislature, they remain unaltered and as an impending block against India's realising the best possible advantages from trade agreements. Further, the aforesaid trade agreements do not form a part of definite economic policy but are haphazard in nature.

Commercial Treaties and Most-Favoured-Nation Clause.

Commercial treaties had served different purposes at different times. Thus when trade was carried on in a foreign

country on personal risk, many nations found it convenient to enter into commercial treaties for safeguarding the traders. During the last century, the most notable purpose served by commercial treaty was to reduce tariff barriers instead of erecting them, the most notable example of this being the *Gobden-Chevalier Treaty* between England and France. In so far as it granted privileges to the goods produced in a particular country, it did away with restrictions to a certain extent. But in so far as these treaties grant privileges to one country against another, they canalise the trade in a particular direction. The chief instrument used for the purpose is customs duty, and different schedules are maintained for different countries according to the treaty conditions. So far as India is concerned, the most notable example of commercial treaty was that entered into with Japan in 1934 on reciprocal basis, which was to terminate on 31st March, 1937. The main provision of the treaty have been summarised as follows: "(i) Both the contracting parties agreed to extend to each other the most-favoured-nation treatment. (ii) At the same time both the parties had the right of imposing or modifying from time to time special customs duties on the imports from each other at such rates as might be necessary to correct the effect of any variation in the exchange value of the yen or the rupee in relation to the rupee or the yen respectively, subsequent to 31st December, 1933. (iii) While both the parties reserved the right to make such changes in their customs tariffs as might be necessary for the protection of their own interests, they were agreeable, when requested to do so by either of them, to enter into negotiations with the object of reconciling as far as possible the interests of the two countries."

But what is the significance of the M. F. N. clause in a commercial treaty and how far did it prove beneficial to the interests of Indian business? The significance is simple enough. When a treaty is being negotiated between two countries, it is but natural that one of the contracting parties is giving more favourable treatment to the other than it has given to any other countries with which it had entered into agreement previously, the effect being that the privileges granted by the previous treaties are nullified by the new one. But when a M. F. N. clause is entered into a treaty, it places

the contracting parties under obligation to extend to each other the full benefit of any lower duties which may subsequently be extended to any other country, thereby extending the new privilege automatically, unless of course the M. F. N. clause is made conditional. So far as India is concerned, the effect of the M. F. N. clause in the commercial treaty with Japan had been ruinous to small nascent industries and handicrafts in India, in so far as the advantage of the clause was taken by Japan which stimulated large exports of manufactured goods like glassware, boots, shoes, hardware, woollen goods, cycles, umbrellas, etc., from that country. It is peculiar that *status quo* was maintained in this respect by the new agreement of 1937 with that country and Japan was assured of the most-favoured-nation treatment for a period of three years. This is the clearest example of how piecemeal agreements with regard to particular goods, like cotton and cotton piecegoods in case of Japan, may not only be evaded in respect of those articles but may be taken advantage of by the stronger rival in other articles as well. A half-hearted agreement is therefore worse than none to the interests of the national economy.

Imperial Preference.

The discussion on imperial preference is placed almost last in a discussion on restrictions on foreign trade; but that does not underrate its importance in the least. The purpose for allocating it at such a place is that it is a subject by itself and is of more permanent interest to the future trade of this country. I have indicated earlier in this chapter that the conscious adoption of a policy of imperial preference, thought without return, and at times with definite disadvantages to the national economy, was first adopted by India and was continued right upto the middle of the last century. The history of Imperial Preference from the beginning of the present century is too well-known to need repetition. But one thing needs be mentioned. India which had maintained adverse attitude to it till 1929-31 all on a sudden began to favour it and the decisions of the *Ottawa Conference* were embodied in an Act of the Legislature in 1932, to be followed by a supple-

ment in 1935. Much thought has been focussed on it both by officials and non-officials who have given different verdicts; but the commercial community of this country has all along been against its adoption. The reason is sufficiently clear. The balance of Indian economy depends, to a very great extent, upon the maintenance of a favourable balance of trade, which must be sufficient to pay not only for the non-visible imports but also to meet the drain. And this favourable balance in export trade depended to a major extent on India's trade with the non-Empire countries. It is true that the volume of exports to non-empire countries declined from what it was in 1913-14. In 1913-14, 37 p.c. of the exports went to the U. K. and British Empire and 63 p.c. to the foreign countries, the corresponding percentages for 1935-36 being 46.4 and 53.6. It was the clear verdict of the *Fiscal Commission* that the conditions of India's foreign trade had not altered so as to suggest a changeover to a system of preferential tariffs; for, under the circumstances, it would involve the raising of existing import duties on imports from other countries which was not deemed proper in the interest of Indian exports. It is suggested that the situation had changed owing to the onset of the depression; but then the adoption of Imperial Preference was not a sane policy. For, the increase in exports to Empire countries was not sufficient to offset the decline in exports to non-Empire countries, as is evidenced by the fact that a huge amount of gold had to be sent abroad in order to maintain the balance of payment. There were other reasons no doubt; but there is no denying of the fact that the adoption of a policy of Imperial Preference was one of them and had reached unfavourably on our export trade. Even to this day the demand of the Empire countries for the Indian products is not sufficient. To-day, as also in early thirties, a more rational policy for India is to explore new markets, a matter which we shall briefly consider under market research.

Not only that; even from the long period point of view, the preferential treatment granted by India was suicidal. It has been recognised by commissions and committees more than once that the solution of the Indian economic problem of unemployment and poverty lies in progressive industrialisation of the country. But a policy which aimed at increasing

the export of raw materials and import of manufactured goods from other countries is nothing sort of a self-denying ordinance. What is all the more striking is that those raw materials and agricultural products appearing in India's export trade, "which did not require any urgent special treatment in foreign markets," were granted preference while "167 items of British imports into India enjoyed preferential duties." The Empire countries, particularly U. K. benefited to a great extent. The following figures are interesting. In the import trade of India, the share of the U. K. was 64.1 p.c. in 1913-14; but during the war, imports from that country declined and after a slight recovery in the early post-war years it declined still further, and in 1926-27, its share was 47.8 p.c. The following years saw a still greater decline, in 1927-8 and 1928-29, the figures being 44.7 p.c. in 1929-30, 42.8 p.c., in 1930-31, 37.2 p.c. and in 1931-32, 35.5 p.c. Then came the *Ottawa Agreement* and imports into India from U. K. recorded an increase, being 36.8 p.c. in 1932-33, 41.3 p.c. in 1933-34, 40.6 p.c. in 1934-35 and 38.8 p.c. in 1935-36. And what was the composition of the imports? They constituted cotton manufactures, iron and steel, motor cars, instruments, mineral oil, hardwares, liquor, paper, etc. India cannot benefit from this type of preference which at times goes to the extent of sacrificing national economic interest for the benefit of imperial products. Therefore, so far as India is concerned, "there is hardly much scope for any static theory of industrial co-operation; and the industrial policy which India is pursuing or will have to pursue in the future is diametrically opposed to any compromise in this connection."

But the position of India vis-a-vis the future of Imperial Preference seems to be extremely delicate. Upto recent times we have seen that the adoption of a policy of imperial preference did not work much to the benefit of this country. We have already said that the exports to non-Empire countries declined but the increase in exports to Empire countries was not sufficient to offset this decline; nor did the Government of India make any effort to explore newer markets; nay, they went so far, as we shall see presently, that they became party to international regulation schemes of certain export goods. True, they did something for the export of raw cotton to Japan; but

that was too negligible a service in view of the extreme callousness in other fields. Under these conditions, Imperial Preference was not a matter of necessity, nor of compulsion, but of choice to the Government, though the Government decision was disliked by the country. The situation has changed since the outbreak of the war and to-day a new type of imperial preference has become not a matter of necessity nor of choice but of compulsion. Since the sterling balances accumulated in India's favour have been blocked and since India has no free hand in the use of her other foreign exchange resources, predominantly dollar, for her own purpose owing to the creation of such devices as conversion of dollar resources into sterling resources, the creation of the Empire Dollar Pool, etc., India's hands in the matter of her imports have been tied down. India is not averse to imports of any kind, nor has she any objection to obtain her requirements from the U. K.; but it is legitimate for her to demand that these resources which are the result of privation, misery and ruin of her millions should be utilised to the best interests of the coming generations. But even in this matter, she has no free choice. The eternal law of business is that the customer does his shopping of the best variety in the cheapest available market. But there are reasons to believe that in certain fields, though not in all, Britain is not the best market for purchase and Indian opinion coming from the business community and expressed in the International Business Conference was all along in favour of making certain purchases in the U. S. A. Nay, they went so far as to urge the need for a separate commercial treaty between India and the U. S. A. That is not all. India's hands are tied not only as to wherefrom to purchase but also as to what to purchase. Indian commercial opinion had favoured the import of capital goods which may help the industrialisation of the country. The attitude of the Government was revealed in the publication of the thousand crore agricultural plan. The results of the Hydari Mission are no more encouraging. Two out of its several objectives are the "imports of such consumers goods as are at present either not produced at all in India or are produced in insufficient quantities" and "procurement of raw materials and working stores required for the manufacture of consumers goods in India."

But what are these raw materials and working stores? They are not capital goods; they are mill stores, dye stuffs, knitting wool, woollen yarn, tinplate, umbrella and bicycle components, industrial chemicals, etc. It is clear from the above list that these goods are not difficult to produce in this country; and so far as the import of industrial chemicals is concerned, its repercussion on newly developed chemical industry of India is to be noted with apprehension. The above list includes only raw materials and working stores. Besides these, India is also to import finished consumers goods like baby foods, vegetable seeds, bicycles, drugs and medicines, paper and stationery items, cotton sewing thread, sewing machines, toilet requisites of all kinds, hardware, glassware, electric household goods, etc., etc. The list is quite succinct and one need not be blamed if he feels pessimistic not only about the future industrialisation of the country but also about the prospect of some old and most newly started Indian concerns. As it is, the figure of sterling balances accumulated in India's favour seems huge enough, but if they are wasted on items as those mentioned above, they will not prove inexhaustible. Hence to-day imperial preference is not a question of necessity nor of choice but of compulsion. The irony of fate is that the position of India as a creditor nation is no better than her position as debtor.*

* Since the above lines were written, India has attained Dominion Status and the new Government has declared its import policy as one restricting the import of consumption goods with a view to preserving and making proper utilisation of foreign exchange resources that have accumulated in our favour. The new import policy falls into three divisions. First, the open general licences, Nos. 1 & 3, applicable to imports from Ceylon, Portuguese possessions in India and any country contiguous to the land frontiers of India have been cancelled. Second, the open general licence No. 7 applicable to import from the U. K. and other Empire Countries with the exception of Canada, Newfoundland and South Africa has been withdrawn. Third, in supersession of this licence, viz., open general licence No. 7 a fresh open general licence No. 9 has been issued.

The effect of the new policy will be that most luxury and consumers goods will be debarred from coming to India but the import of capital goods which are defined as any plant worth more

Bilateralism and Multilateralism.

Although multilateralism as a device is to be found in the earlier developments of international trade being utilised for the standardisation of trade practices, procedure, rates and similar other matter, as a device to influence international trade—both its volume and direction,—bilateralism and multilateralism became very much important since the world depression. The Indian business community also, in their effort to maintain the trade balance, began to urge the necessity for bilateralism. For, economic nationalism of India's foreign customers, especially in Europe, was viewed with great alarm in this country because of the fact that our export trade with these countries was more important, and the government was being urged again and again to enter into bilateral agreements with all important countries with which India has commercial relations. Various arguments have been put forward against bilateralism, the most important of which from Indian viewpoint is that India does not possess the necessary instrumentality. The argument is often supported by the results realised in the Ottawa Agreements with Empire countries. But when a case is put forward in favour of bilateralism, it is based on the repudiation of imperial preference. It is of course true that an Independent India moulding her fiscal policy is in the most advantageous position; for in that case the Government of India would not feel any delicacy when communicating a trade treaty with England or her dominions. At present her hands have been tied up by the various commercial safeguards and the so-called fiscal autonomy is nothing else than a myth. But even then when bargaining with a non-Empire country it may fairly be expected that the government would not be overpowered by any such delicacy as they feel at present when dealing with Empire countries and

than Rs 25000 will remain unaffected. Naturally it will affect our import from England adversely, which is our principal supplier of luxury and consumption goods. The import from the U. S. A. will however not be affected; on the contrary, there will be greater demand for goods from that country than can be available owing to the shortage of dollar.

would enter into treaties that may be fair to the commercial interests of India.

Under the changed circumstances of the war, bilateralism and multilateralism have assumed a bit different importance. Since the sterling resources of India which has accumulated in England have been blocked, the only solution of the problem is to have it back by means of some bilateral settlement between England and India. Elsewhere I have argued that "the problem can best be tackled by separate agreement rather than by looking at it from an international perspective." It should be realised that this type of bilateralism is all the more suicidal; for, it would divert all our purchases into one channel, whether we like it or not. Therefore, a much better solution of our problem would be to enter into a bilateral agreement with England which would provide for some measure of multilateral convertibility, which is vital to the economic interests of the country. This multilateral convertibility should not be restricted to Empire countries and other non-Empire countries of the sterling area, but should embrace non-Empire countries as well, particularly U. S. A. Indian opinion has been all through in favour of the creation of a dollar fund of her own and it looks upon America as the most convenient market for her purchases, and this can only be satisfied by some such device as bilateral agreement with England providing for multilateral convertibility of our sterling resources. But where scramble for market is the major issue, any such device would not be acceptable to England nor would the Government of India move in this matter. But if goodwill and sincerity prevail, the multilateral convertibility would not be a difficult matter, and the proposed World Bank may provide the necessary medium. the debtor country borrowing from the Bank and utilising the proceeds derived therefrom in repatriating the sterling obligations, the creditor countries being thus enabled to utilise the foreign exchange resources according to their needs.

Commercial Safeguards.

Another type of restriction, unparalleled, in the history of any independent country may be termed commercial safe-

guards, the phrase being used in a special sense. When an independent country adopts some safeguards, it implies that the country in question is sheltering some of her interests; not so in case of India. Safeguard in our case implies safeguarding of some interest other than Indian. Thus Section 12(1)(f) of the *Government of India Act, 1935*, provides the Governor-General with responsibility for "the prevention of action which would subject goods of United Kingdom or Burmese origin imported into India to discriminatory or penal treatment." In the words of the critics, "Except for the all too powerful impulse of British Imperialism—and the memory of the treatment given to Indian goods, and Indian aspirants for acquiring industrial technique in British establishments—there is no reason why this Special Responsibility should be so specifically added. India can use no weapon against British competitors, which the Governor-General cannot, in effect, stultify or veto, whether in the legislative or in administrative field." Since the attainment of Dominion Status by India, these safeguards have been removed.

Indian Trade and International Regulation Schemes.

Apart from the various disabilities, restrictions and safeguards imposed on Indian trade which we have discussed in the previous section, there is still another disadvantage from which India as one of the major agricultural countries of the world suffers. This is due to the adoption of international regulation schemes. So far as countries producing manufactured goods are concerned, we know that the formation of some international combines has at times striven to attain the desired result of output regulation, or price fixation or market distribution. In agriculture and raw material producing industries, the regulation schemes have operated and it is to some of them that we shall divert our attention in so far as they interest us in Indian foreign trade. Two facts must however be borne in mind in this connection. In the first place, whatever success these regulation schemes have attained, it has been due to the solidarity rendered possible among the producing countries as a result of the great depression, which left agricultural and raw material producing countries into

greater crisis than those predominantly manufacturing or having a more or less balanced economy. Secondly, the participation of the Government of India in some of these schemes, it is strange, has been disadvantageous to the interest of the country which they represented in these international conferences. These conferences are the clearest proof as to what extent a dependent country may submit not to the dictates of the dominating country but to that of third party.

The most interesting case is that of sugar. In order to realise that injustice done to India, we must realise what a "free market" is, for, although the word "free" in dictionary sense has a good connotation, yet at times it is undesirable, as it happened in case of India which though politically unfree was declared a free market for the exploitation of outside producers of sugar. For purposes of comparison of consumption with production, the world has been divided into three parts (*Tariff Board Report on Sugar Industry, 1938*):—

(a) Countries which consume sugar but produce none within their own territories, e.g., Norway and Greece.

(b) Countries which produce sugar but do not produce enough to meet their entire demand and have to import, e.g., U. K. and U. S. A.

(c) Countries which produce more sugar than they consume and have a surplus for export, e.g., Cuba, Germany and Java.

The first two categories of countries constitute "Free market" and although India, at the time of the International Sugar Conference of 1937, was producing at least equal, if not more, to her consumption needs, she was classified as a "free market." In 1930-31 this so-called free market amounted to 6 million tons. In 1938 it was half of that in 1930-31 or about 10 p.c. of the world production, the remaining 90 p.c. being markets closely protected in the interests of domestic producers. The depression which led to a shrinkage in the world demand for sugar was followed by a vast surplus of sugar production and, to meet the situation, the *Chadbourne Plan* was formulated between the producers in Cuba, Java, Germany, Czechoslovakia, Poland, Hungary and Belgium.

The plan was intended to secure joint restriction of exports and production with a view to liquidating the existing stocks within five years. But the restriction on exports did not succeed in raising the world prices, because it stimulated production in those countries which were not party to the agreement, particularly U. S. A. and U. K. with its colonies and India.

The International Sugar Conference concluded in London in 1937 a comprehensive agreement for the regulation of world prices and production. Regulation is to be effected by means of export quotas and general undertakings which comprise the prevention of excess production in the event of a rise in prices in the free market, the adoption, as an object of national policy, of a reduction in the disproportionate fiscal burden on sugar, action to increase consumption and the promotion of reciprocal agreements. Among the non-exporting countries, the U. S. A. will continue to import at least in the same proportion as it was importing. The U. K. will limit home production to 618000 metric tons and export from the colonies to 965254 metric tons. Australia is given an export limit of 406423 tons and South Africa one of 209000 tons. India was prohibited seaborne exports to places other than Burma. Export of Indian Sugar by sea is shown below:—

(In tons)

	1934-35	1935-36	1936-37
Ceylon	... 360	376	475
Burma	... 2341	1300	18762
Other Colonies	... 3	13	44
...	2704	1689	19281

Indian opinion was hostile to this agreement particularly so, because India at this time was suffering from overproduction and was facing an impending collapse when all on a sudden the above agreement came into force. It is well-known that sugar industry in this country has developed since the depression, and within a few years the whole country became self-sufficient, nay, India was able to supply the foreign

market. At this stage the Agreement came as a bolt from the blue. Whatever that may be, Indian opinion has all along been hostile to the Agreement and was urging for its termination till its expiry in 1942. It is difficult to imagine what the Government would have done in normal circumstances. But in view of the opportunities afforded in the export markets for Indian sugar on account of the loss of Java, Philippines and other important producing centres, and the utter uselessness of continuing the sugar agreement when many of the signatories had ceased to exist, the agreement was not renewed after its termination.

In another case India became a party to the international regulation scheme, *viz.*, in case of tea, which proved beneficial to the industry. The year 1932-33 was one of the worst for the tea industry. The world trade depression had its part; but the main reason was the overproduction, with the consequence that producers of tea all over the world were faced with declining prices and accumulation of stocks. So far as India was concerned, the preferential treatment granted to Indian tea in Empire countries was not sufficiently effective to prevent the consumption of cheap Java tea in these countries. To solve the problems facing the world tea industry, an International Tea Committee was formed whose function it was to regulate exports from India, Ceylon and East Indies (Dutch) by quotas based upon the export figures for the year 1931. It has also arranged to levy a small duty on tea production of the countries concerned, the proceeds being utilised for carrying on propaganda, on a co-operative basis, in favour of the consumption of tea. The stock position in London, undoubtedly the most important single factor in the trade, was also controlled by the committee till the outbreak of the war in 1939. The international scheme was given effect to in India by the passage of a bill by the Indian Legislative Assembly in 1933. Consequently the industry has been able to enjoy more stable conditions. The export quota which was fixed at 82½ p.c. of the standard exports in 1935-36 rose steadily to 92½ p.c. in 1938-39. Due to accumulation in stocks and decline in prices, the quota for the following year was fixed at 90 p.c. But this reduction in export quota, along with increased consumption, had the effect of placing the

industry again in a favourable position in the world market even before the outbreak of hostilities. A comparative table showing the quantity exported from various producing countries during the last three years of the revised control which came into operation in 1938 is given below:

(Source: *Investors' India Year Book* 1942-43).

(In millions of lbs.)

Country	Standard Export.	1935 82½ p.c.	1936 82½ p.c.	1937 87½ p.c.
India	382594779	315640692	315640692	334770432
Ceylon	251522617	207506159	207506159	220082290
Neth. East				
Indies	173597000	143217525	143217525	151897375
Total	807714396	666364376	666364376	706750097

Country	Standard Export.	1939 95 p.c.	1940 Partly 95 p.c., 92½ p.c. & 90 p.c.	1941 110 p.c.
India	383242916	364080770	356096543	421567208
Ceylon	251588012	239008612	233767195	276746813
Neth. East				
Indies	173597000	164917150	161300546	190956700
Total	808427928	768006532	751164284	889270721

Over and above the exportable quota, each country was permitted to make its own arrangement, until recently, for the production of additional quantity of tea for internal consumption. In India the quantities of tea available for consumption over four years ended 1937 were approximately as follows:

(Source: *Investors' India Year Book* 1942-43)

1934	1935	1936	1937
lb.	lb.	lb.	lb.
60000000	65000000	67500000	80000000

Since the outbreak of the war, conditions in tea industry have changed considerably. In U. K. the entire tea trade has passed under the control of the Government and the British

Government have contracted to take the bulk of production from allied sources. In India a Tea Controller has been appointed to administer the emergency tea control scheme. Under the emergency scheme both the export quota and internal consumption allotment had to be raised, the former from 95 p.c. in 1939 to 100 p.c. early in August, 1941 (during the intervening period they were sometimes reduced to 90 p.c. and 92½ p.c. for temporary period), and to 110 p.c. in November 1941 and to 125 p.c. in January 1942, and the latter from 17 p.c. to 22 p.c. in 1942.

Apart from these two regulation schemes on an international basis in which the interests of India were involved, there were various other schemes in which India was neither a party nor interested. One such scheme was formulated in connection with the cultivation and export of wheat in 1933-34, when the wheat exporting countries came to an agreement as to export quotas and limitation of acreage under production and the wheat importing countries agreed to lower import duties on wheat, to delimit domestic production to the current acreage at the time when the agreement came into force and to increase import quotas if a certain price-level was reached. The agreement was however not so much of a success in view of the fact that some countries like Argentine did not give effect to it, while the importing countries did not restrict production. Another important scheme worth mention is the *Stevenson Scheme* controlling the production of rubber in Straight Settlements, Malaya States and Ceylon, restriction being based upon a system of export quotas calculated as a percentage of the "Standard production," which was calculated on the basis of the output of each producer during the year ending 31st October, 1930. The scheme was a failure in view of the fact that the non-participants took advantage of it and increased their own production and export. Therefore in 1937 a new international rubber regulation scheme was brought into existence which embraced about 97 p.c. of the world production, the control being vested in the hands of an International Rubber Regulation Committee. Among the international schemes for the regulation of raw materials, mention may be made of that connected with tin production which was the most successful

in this field. The problem of over-production has cropped up since the end of the first world war and the situation deteriorated with the great depression. Therefore in 1929, a Tin Producers' Association was formed not for controlling supply, but for finding newer uses for tin, and was followed in 1930 by the formation of an International Tin Committee by the Governments of British Malaya, Dutch East Indies, Bolivia and Nigeria, with a view to regulate the industry in these countries. The Committee prescribed both export quotas and limitation of production. Subsequently, the scheme received the support of most of the producing countries. With a view to raise the price from the uneconomic level to which it has sunk, the Committee organised a Buffer Tin Pool whose function it is to receive from each producing country certain quantities of tin and to withhold them from the market until the price level has gone above £165 per ton.

The question of the revival of international trade has been attracting the attention of experts since the end of the second great war. Sometime back an international conference was called at Geneva* to consider the situation at which talks about international tariff negotiations were heard. Our experience with international tariff negotiations and regulation schemes being what it is, any such talk makes the interested parties apprehensive. This is particularly true of the industries that have come into existence during recent years, such as, engineering, heavy chemicals, electricals, non-ferreous metals, etc. In any international tariff negotiation, the case of these new industries should never be neglected but should be protected. Foreign countries are already anxious to enter the Indian market, which if allowed would destroy these newly started industries. Hence in any future international negotiation regarding tariff, the interest of the newly started industries must not be neglected. Not only this; quantitative import restrictions should also be recognised in the case of those countries in particular who want to develop their economic resources by utilising their limited exchange resources. This is also true of our country. Our sterling resources are hard-earned and must not be squandered in any

* See Appendix.

way but utilised for the economic development of this country and this should not cause heart-burning among big industrial powers. This clause should also form a part of the future World Trade Charter.

Risks in Foreign Trade.

Whenever trade goes beyond the political boundaries, the normal risks of trade are intensified. It is not that risks do not exist in home trade; they are there. But the intensity of the risks increases as soon as the political boundary is crossed. This is not all; some new risks which are conspicuous by their absence in home trade crop up. The most important of these types of risk are those connected with the foreign exchange. It is no doubt true that the currency of a country has two values—external and internal—and the latter value is as much fluctuating as the former one. But the fact remains that slight changes in the internal value of currency are not felt so much as slight changes in the external value of the currency. For a slight change in the latter leads either to automatic or to conscious adjustment in the rates of exchange.

Credit Risk.

The very first risk to which one's attention may be drawn is connected with credit sanctioning. Credit risk, does not simply mean buyer's credit; it also means seller's credit. So far as the seller is concerned, the question arises as to whether he has credit enough to fulfil the contract. We have seen in connection with our study of the export agencies in agricultural products that most often the contract between the purchaser and the seller is non-mutual in character, the disadvantages being placed against the seller. Thus when the quality of the goods contracted for is superior to the quality agreed upon, the seller receives no premium; but when the quality is inferior, the seller has to suffer because of deductions from prices or various other troubles. We are not concerned with the efficacy of this system of contract. But it is apparent that the seller's side of credit is more emphasized upon in the present case and before entering into a contract for the purchase of anything, the purchaser must see whether the con-

tracting party is sound enough so as to be able to fulfil the contract.

The other aspect of the credit risk, and the more important one, is concerned with the buyer, and the seller is to be sure that the party in question is sound enough and in a position to honour the obligation it has incurred by purchasing goods on credit. It is wellknown that the sources obtaining credit information include customer's reference, banker's opinion, commercial enquiry agent and publication, both official and non-official. Of these, banker's opinion is the most important so far as the Indian customer goes and the banker's opinion in question is the opinion given by the exchange banks. It has been an agelong complaint by the Indian importers that the exchange banks which are all foreign give poor references regarding Indian commercial houses to enquiries from abroad and give better references as to foreign commercial houses even though actually the latter are in a lower business standing. When this point was brought before the *Indian Central Banking Enquiry Committee*, the exchange banks tried to justify their position on the ground that this difference in treatment was due to the unwillingness on the part of the Indian commercial houses to supply the banks with audited balance sheets. But this argument does not stand on solid ground in view of the fact that every company registered under the *Indian Companies' Act* must have audit and give publicity to its balance sheet. It may be argued that the exchange banks want the audit to be done by an auditing firm approved by them. But if they actually want this, there is no logic in this case as well, in view of the fact that the auditors are people approved by the government. However, this was denied by the exchange banks who stated that they only wanted accounts to be audited by auditors who are on the approved list of the government. But these were not the real reasons for the partial treatment. The real reason however came out and it was that the managers of the exchange banks, being foreigners, are not able to keep themselves in close touch with their Indian clients and have therefore to depend for the information regarding their financial standing upon the reports of the subordinate members of their staff or brokers or shroffs.

The other sources of credit information referred to above are not either properly developed or are conspicuous by their absence in this country. One very important source of obtaining this information in advanced commercial countries is the commercial enquiry agents. Some of these firms issue periodical credit lists not only for home concerns but also for some foreign countries, the names being arranged according to the standing of the different firms and the list being supplied regularly to subscribers. Apart from specialising in supplying credit information to the subscribers for a few countries in the published list, they also maintain extensive files of reports on firms in all important trading countries, which are supplied to subscribers when required by them. In recent years, they have extended the line of their activity and have included in the services rendered by them the collection of bad and doubtful debts at home and abroad, and are prepared to tender advice to unpaid creditors as to whether they should take to legal proceeding for the realisation of the due amount or whether they should bring pressure by some other means.

Another important source of obtaining credit information in all countries, India being no exception, is the Government Department of Commercial Intelligence. The function of this department of the Government of India is to provide "a convenient link between the government and the commercial public and is responsible for the collection and dissemination of commercial information with a view to the promotion of Indian trade, especially on the export side. It answers trade enquiries, effects trade introductions, disseminates trade information regarding trade openings in other countries to firms in India and circulates information regarding Indian produce and manufactures to merchants abroad who are likely to be interest in such information."

In advanced countries, like England, U. S. A., Germany, etc., credit risk may often be insured by taking up floating policies available for certain lines of trade, the procedure of taking a policy being very similar to that in case of marine risk policy. Policies of this type are issued by underwriters and insurance companies, some of the latter specialising in this class of business, e.g., The Trading Indemnity Co. and The General Trading and Finance Co. in Britain. Sometimes, as

in England, a Government Department may perform the function of insurer, the object being to facilitate the financing of exports, where the importer's status is not sufficiently well-known for the exporter's bank to be prepared to advance funds against order. In England the Export Credits Guarantee Department issues two types of policies, *viz.*, comprehensive guarantee and specific policies. Comprehensive guarantee is available for shipments to all overseas buyers. The exporter has to submit details of his estimated shipments for coming 12 months, his export trade for previous five years, his bad debt experience, the importer to whom goods are sent and the nature of the goods. The Export Credits Guarantee Department then assesses the risks and quotes premium. The premia so quoted are of two types—one in which the whole risk is borne by the Department, subject to an agreed maximum and the other where a certain proportion of the loss calculated with reference to his previous bad debts experience is borne by the exporter himself, the rate charged in the latter case being lower than that in the former. Specific policies are available for a part of the exporter's business, the department agreeing to cover an agreed percentage of unpaid bills drawn on the buyers, the maximum being 75 p.c. Since the risk is not so well-spread the premium charged is consequently high. According to the *Commercial News* of Los Angeles, the chief characteristic of export credit insurance system is that by purchasing this type of protection, a small exporter can be protected against the risk of loss in two ways: first, by reason of non-payment for goods delivered to a foreign customer, he would be enabled to make sales and extend credit to more sound and legitimate foreign accounts to which he, otherwise, might hesitate to sell, because of difficulty in securing adequate informations to judge their true credit standing; secondly, he would be able to turn over that portion of the working capital which otherwise would be tied up in goods sold to foreign customers on credit terms to six months or a year or more. Moreover, after the acceptance of the goods abroad the debts would be guaranteed to the extent of the insurance coverage against the risk of nonpayment. With this backing his drafts drawn on foreign customers would find a steadier market than before. A comprehensive development on these lines cannot

at present be suggested for India though a beginning may be made and the government can do a lot by taking at least an active part in the collection and dissemination of credit information.

Publications, both official and non-official, have at times served the purpose of supplying credit information. In India, both the official and non-official agencies are more or less concerned with the supply of trade information rather than credit information. In this respect, therefore, there is a big gap which needs be fulfilled.

Exchange Risk.

Next we shall turn to another variety of risk which is known as Exchanged Risk. The nature of the risk involved may briefly be explained. When the invoice and the bill of exchange are prepared in the currency of the buyer, the seller runs the risk that the eventual conversion of the buyer's currency into his own may bring him a smaller amount than he anticipated in terms of his own currency. Thus if the invoice and the bill of exchange are prepared, at the exchange rate of Re. 1 = 1s., in Indian currency, and if at the time of the receipt of payment the seller receives 10d. instead of 1s. for each Re., then he sustains a loss 2d. per Re., although, in terms of Re., he has received the same amount. If the same bill is drawn in the currency of the seller, say pound sterling, at the exchange rate of Re. 1 = 1s., and if the buyer, at the expiry of a stated period, has to purchase sterling at Re. 1 = 10 d., instead of 1s., the seller in purchasing the same amount of sterling has to sustain a loss of three annas and two and two-fifth p^yies for each shilling. On the other hand, if the rate of exchange, instead of coming down, goes up, the reverse will be the case. Let us see what happens in case Re. 1, instead of being equal to 1s., becomes equal to 1s. 2d. In this case if the bill is drawn in the currency of the buyer, the seller will get more in terms of his own currency and will therefore be at advantage over the buyer. If, on the other hand, the bill is drawn in the currency of the seller, the buyer benefits at the time of payment in so far as for the same amount of pound sterling he has to spend less in terms of

rupees. The risk is multiplied in case of trilateral exchange. Thus when India has to send some commodities or purchase others through the intermediary of London agents, money is being exchanged twice. Rupee in sterling and sterling into franc or mark or any other European currency, and the duplicate transaction multiplies exchange risk.

The problem of exchange risk, although not unknown, did not assume much importance before the first world war in view of the automatic adjustability of the gold standard and the fluctuation of the exchange rates between two specie points. But after the war the world was faced with new conditions in which exchange risks had multiplied and the specie points were not sufficient check to the fluctuation of the exchange rates. The subject assumed very great importance not only in theoretical discussions but also in practical measures to meet the situation. The *Memorandum on the Improvement of Commercial Relations*, etc., contains a mine of theoretical discussions contributed by the best brains, various arguments have been put forward both for and against the question of flexible parties, widening of the gold points, etc., etc. Whatever the efficacy of these theoretical considerations may be, one thing is clear, *viz.*, that there is "a growing understanding of the insufficiency of some of the older methods of ensuring a monetary balance." In practical field, various efforts have been made at minimising the effects of exchange fluctuations by the adoption of exchange control devices. These devices have no doubt varied, being mainly divisible into two types, the British type and the German or "rationing" type; but there is nothing to say in favour of one and against the other, in so far as the emergence of a particular type of exchange control was the result of the peculiar circumstances of the country in question. But then there is no essential difference and the British type is not so much lenient as it is often made to be; for the device of Exchange Equalisation Account and the secrecy under which it is operated are sufficient proof of the fact that the hand of the British Treasury, though invisible, is effective enough. In the words of Ohlin, "Monetary authorities (in England) have on many occasions intervened not only on spot market but also with purchases or sales on forward market. By preventing very large discrepancies

en spot and forward quotations, they have perhaps been able to prevent the spread of a lack of confidence in the value of some threatened currency. They have also been able to make the speculators 'burn their fingers.'"

(*American Economic Review*, 1937, Supplement.)

The above measures at minimising exchange risk have been taken by the state and are aimed at against wide fluctuations. When fluctuations are quite normal, smaller measures may be quite sufficient for the purpose and the monetary authorities in different countries have not remained indifferent in this respect. When debts are immediately payable, the following covers may be available against exchange risk. The importer can arrange with his bank to purchase foreign currency from the latter at almost the same T/T rate at which the bank has purchased it, a small addition being made to allow for the bank's profit and expenses. In this case the importer does not lose in so far as he is sure to get the foreign currency at a certain rate. The exporter also can cover himself against any exchange risk adverse to him by selling the exchange to his banker, the currency bills with attendant documents being sold to the bank at rates of exchange which allow for the bank's commission and other expenses, and the risk of any future adverse fluctuation in the rates of exchange being borne by the bank. Where the debt is however not payable immediately various covers may be available. Thus the importer can purchase foreign currency immediately which he will have to pay at some future date. He need not receive the foreign currency from the bank at once; the bank will hold it for him, until required, with its agent in the centre in which the payment is to be made. In the same way the exporter can cover himself by selling the usance bill to the bank not exactly at market rate of exchange but at a slightly higher rate so as to cover risk, profit, collecting and discounting charges, etc. But the most scientific device that has been adopted is known as Forward Exchange, which, even without limiting the fluctuations of exchanges, "provides an interesting and ingenious way of avoiding unexpected losses arising out of them. In forward exchange, the dealers contract to purchase and sale a certain amount of foreign currency one month, two months' or three

months' hence at to-day's spot rate of exchange, whatever spot rate might have become by that date. The forward will not exactly be equal to to-day's spot rate but will differ from the latter by a small amount and will be quoted at a premium or discount on the spot rate according to the pressure of demand for the currency of a particular country. So far as the trader is concerned his position is secured. But in selling currency forward, the banker runs a risk, according as what the rate of exchange is going to be three months hence. Therefore when a bank agrees to give delivery of currency at some future date, it is wise for it to purchase the same amount immediately in spot market and keep that sum in the country in which payment is to be made, until the contract matures. To keep this sum on deposit may involve a loss of interest and in that case the forward currency will stand at premium. If however the rate of interest earned on deposit is high so as to leave a margin to the bank, the bank will naturally grant a discount.

Now let us turn to the Indian side of the picture. In India the conscious manipulation of the ratio is quite old. At times the rupee is linked to sterling, at others to gold; at times the rate of exchange is 1s. 4d., at others 1s. 6d. It is well-known how the gold exchange standard had come into existence in India and was maintained by the Council Drafts System during the pre-war period. But difficulties arose with the outbreak of the war. As soon as the first shock of the war was over, exports revived and the demand for Council Bills increased. Within a short time, the sale of Council Bills resulted in the depletion of the rupee reserves in India. Certain measures were adopted to meet the situation and the exchange rate was fixed at 1s. 4½d. in January 1917. But the measures proved inadequate owing to the remarkable rise in price of silver and it became impossible to maintain the rate of exchange at 1s. 4d. when the market value of the silver content in the Rupee was not less than 1s. 8d. and even more. The only solution suggested by some people that the loss be debited to the Gold Standard Reserve was not accepted and the rate of exchange began to rise, thereby reaching the peak of 2s. 11d. in the early months of 1920. The tide then turned when the demand for Council Drafts had ceased and there was

a strong demand for Reverse Councils. The Government accepted recommendations of the *Smith Committee* and adopted the exchange rate at 2s. gold. But the Government effort to maintain this rate was a failure. For some time owing to the heavy demand on the part of exporters to discount their export bills, and thus to obtain rupees, as early as possible, thereby protecting themselves from the rise of exchange which was expected every now and then, there was a rush of the Indian exporters which itself led to a rise in the exchange rate as high as 2s. 10½d. The abnormally high rate of exchange favoured imports and the purchasing power which was sent up during the war was released in torrents. The boom was all the more stimulated by speculative activity in exchange transactions. The balance of trade which had been favourable during the war took a reverse course. The exchange rate began to decline and reached the lowest level of 1s. 3d. in 1921. Thus both the specie points had broken down and efforts at stabilisation were nullified. We are not concerned here with the currency history; but we cannot neglect the risk arising out of exchange fluctuations in so far as it affected the commercial community of this country. The effects were three-fold. In the first place, the sterling balances which had accumulated during 1914-19 were squandered, partly due to the foolishness of the Indian public in their demand for silver, at a fabulous price, which after the war lost much of its monetary significance *vis-à-vis* gold, but mainly due to the short-sighted policy of the Government which at once acceded to the public demand and "set up the whole theory of the requirements of trade and of the obligation to sell reverse councils, which transformed the problem of proper utilisation of our foreign balances into one of acquisition of silver for internal circulation and management of the rupee ratio for external purposes." Secondly, the high rate of exchange worked as a stimulus for placing orders with foreign countries for the import of plants, machinery, etc. The commercial community had placed their faith in the ability of the Government to maintain the ratio at 2s. gold. But when the Government failed to do so and took shelter in the policy of masterly inactivity, the commercial community, which had not taken any usual precaution against exchange risk, was placed in ruins.

For they had contracted to receive their goods on the expectation that they would get 2s. gold in exchange of Re. 1; but when the exchange collapsed, the expectation evaporated and the whole investment proved grossly uneconomic. And thirdly, the vexed ratio question which originated from this time has come to stay even to this day and this aspect of the problem, so very important in the successful conduct of foreign trade, has not yet been solved.

The subsequent history of ratio controversy is sufficiently well-known to need recapitulation. Suffice it to say here that in spite of the protests of the Indian commercial community, the ratio was fixed at 1s. 6d. sterling, instead of 1s. 4d. which had been regarded in this country as the natural rate. It is of course true that there is no such thing as sanctity about the natural rate nor is it easy to say what a natural rate is under particular circumstances. But one thing remains clear. When the whole world was moving towards devaluation for giving ease to their foreign trade in view of the impending depression, Indian currency was actually over-valued and was sheltered by the export of gold from this country. Whatever the merits or otherwise of the gold export, the above factor remains clear and what the Government of India should have done by economic means of devaluation of the rupee and exploring possibilities of stimulating exports was achieved in a non-economic manner.

In view of the abnormal increase in exports and consequent one-sided pressure on the exchanges since the outbreak of the war in 1939, the Government of India instituted exchange control with a view to stabilise the exchange rate. Apart from this, the Reserve Bank announced its decision to deal in forward sterling. For, owing to the difficulty of obtaining cover in London for positions other than spot and the rise in the discount rates there, banks were reluctant to do forward business for the first few months of the war. The Reserve Bank therefore announced that it would be prepared in future to purchase sterling for forward delivery extending over a period of 90 days at a higher rate. This, along with other measures, has resulted in a more or less stable exchange rates:

Two new developments after the war may now be noted in brief. They are, first, the de-linking of the Rupee from sterling

and second, the establishment of International Monetary Fund with a view to secure stability of exchange rates throughout the world and to stop the race of currency depreciation. As a result of the de-linking of the Rupee from sterling, Rupee has become an independent currency and may be linked with the monetary unit of the International Monetary Fund. For this purpose, in place of sections 40 and 41 of the *Reserve Bank of India Act*, a new section has been substituted as follows: "The Bank shall sell to or buy from any authorised person who make a demand in that behalf at its office in Bombay, Calcutta, Delhi or Madras, foreign exchange at such rates of exchange, and on such conditions as the Central Government may from time to time by general or special order determine, having regard so far as rates of exchange are concerned to its obligations to the I. M. F. provided that no person shall be entitled to demand to buy or sell foreign exchange of a value less than two lakhs of rupees." Section 17 of the Act is also amended so as to enable the Reserve Bank to buy and sell securities issued by the Government of any country outside India which is a member of the I. M. F. The rate of exchange is no longer fixed by the Act but is left to the Central Government which is to determine the rate subject to such conditions as it might deem necessary consistent with the obligations under the I. M. F. Turning next to the second question, *viz.*, the establishment of the I. M. F. with a view to secure the stability of exchange rates, the prime object of the Fund is to "promote international monetary co-operation through a permanent institution which provides machinery for consultation and collaboration on international monetary problems." The par value of the currency of each member is to be expressed in terms of gold as the common denominator or in terms of the U. S. dollar. Each member undertakes to collaborate with the Fund to promote exchange stability, to maintain orderly exchange agreements with other members and to avoid competitive exchange alterations. The Fund provides machinery for changing the par value of a member's currency only on the member's proposal and after consultation with the Fund. To some extent the members are granted individual action provided it does not affect the international transactions of members. But sanction may be evoked against

members for making unauthorised changes in par value. These measures will go a long way to minimise exchange risk in international trade.

Transfer Risk.

Another variety of risk that arises in foreign trade is known as transfer risk. Here the exporter runs the risk that the country of import may find itself, at sometime between the export of his goods and payment for them, unable to meet its obligations. The intensity of the risk is not the same everywhere but varies according to circumstances. So far the world has experienced three types of transfer risks. In the first place, the risk may arise from the over-valuation of currency as was the case in early thirties with the Gold Bloc. The over-valuation resulted in the adverse balance of trade from which France and other countries of the Gold Bloc suffered till 1936 when franc was devalued. The experience of the over-valuation of the Rupee and consequent outflow of gold is no less remarkable. In fact, the over-valuation of the Rupee, side by side with the depreciation of currencies in other parts of the world, thereby creating a greater gap between Rupee and foreign currency was one of the reasons—though not the only one—of the disappearance of our export surplus, and the balance of account had to be maintained, as in the case of the Gold Bloc, by the export of gold. The second experience arose out of the reparations payments, whereby the vanquished nations after the first world war were required to transfer a sum greater than their normal import surplus. This had a very severe strain on the economies of the vanquished nations. In such a case, if the country is on a gold standard, it is compelled to forsake it, go to paper in its place and devalue the currency to a lower rate. If it is already off gold, the only course is to declare a moratorium or a standstill agreement. A third type of transfer risk has been experienced by India in the present war. This is concerned with the accumulation of sterling in England in India's favour and their blocking for the war and transition period. It is a poor sight that the seller is in a helpless position as regards the utilisation of these balances. It is suggested that if abnormal war balances are

liquidated by a flow of additional exports from the debtor to the creditor country, no special problem arises. It is quite true so far as the debtor country is concerned; but not so in case of the creditor country. For if this flow of additional exports from the debtor to the creditor country be in the shape of consumption goods, it will do a permanent harm to the industrial development of India. Besides, why should India be forced to purchase in the English market against her will? The eternal law is that the customer purchases in the cheapest market available. The method of utilisation of sterling balances should also be left to their rightful owner. Dominions like South Africa and Canada have, despite their racial attachments to mother country, not postponed the question of utilisation of sterling balances until the termination of hostilities but have taken care to see that their immediate requirements are met and that their vital interests adequately safeguarded in all transactions relating to sterling. India is denied this privilege even.

Risk at Sea.

Finally, we shall touch upon another risk, *viz.*, risk at sea. The nature of the risk involved in sea voyage is well-known and the need for insurance is apparent enough. Here therefore we shall simply consider, in brief, how far provision has been made in India for the removal of this type of risk. But before we do that, we may mention in brief the procedure of taking a policy in marine insurance. Sometimes the marine insurance companies transact the business directly; but more often the transaction is carried through agents whom the companies appoint with general or limited powers to bind the latter on risks. They are usually provided with a schedule of rates of premium and limits as to the amount insured applicable to different classes of business transacted. The method adopted in effecting a contract of marine insurance differs from that employed in other branches of insurance business; for, it is effected through a broker who, on receipt of instructions from his principal, makes out an abbreviated memorandum of risk, known as original slip. The broker then takes the original slip and offers it for subscription to a company underwriter. If the risk is acceptable to the underwriter, he

quotes a rate per cent and if it is accepted, it is entered on the slip. The underwriter then writes his line. Where large amounts are involved, the broker may have to take the slip to several underwriters to secure subscriptions till the full amount is covered. Be it noted however that the original slip has no place in the eye of law. So also the cover note which the broker forwards to his client on completion of an insurance. Both the original slip and the cover note are binding in honour only. When the insurance has been effected with a company, on receipt of final instruction from his client, the broker makes out a closing slip, alternatively known as a forward or definite slip, which states at greater length full particulars of the risk as indicated in original slip.

In India the business of marine insurance is a virtual monopoly of non-Indian concerns. An idea of the share of the insurance business transacted by Indian and non-Indian concerns can be had from the following table:—

	(in crores of Rupees.)		
	1938	1939	1940
<i>Life Assurance—</i>			
Sums assured with Indian Cos. ...	204	215	225.51
Sums assured with Non-Indian Cos. ...	94	56	60.12
Premium Income ...	15.6	14.3	13.99
Premium Income of Indian Cos. ...	10.5	11.3	10.69
Premium Income of Non-Indian Cos. ...	5.1	3	3.30
<i>Non-Life Insurance—</i>			
Total net Premium Income ...	2.82	3.37	3.61
Total net Premium Income of Indian Cos. ...	0.89	1.02	1.18
Total net Premium Income of Non-Indian Cos. ...	1.93	2.35	2.43
Total Fire Premium Income ...	1.38	1.52	1.45
Total Marine Income ...	0.52	0.95	1.31
Total Miscellaneous Premium Income ...	0.92	0.90	0.85

The whole of the above table is not relevant for our present purpose. But yet it has been given in order to have a glimpse at the comparative position of the Indian and non-Indian concerns in life as well as non-life business. It will be seen that while in life business, Indian concerns predominate, in other fields, the non-Indian concerns have a major role. This should not however be taken to mean that Indian firms are unwilling or unfit to transact other types of business. The main reason is one of connection and influence. We have already seen that about 80 to 85 p.c. of our foreign trade is in the hands of non-Indians and it is but natural, though antagonistic to the national interests, that the firms in foreign trade will give their support to their own people. The attitude of the overseas importers is no less a determining factor. Thus the overseas importers, say, in England, stipulate in their letters of credit that insurance should be effected with a British Company, with the consequence that the exchange banks do not accept documents unless the goods are insured with a British Company. No less responsible is the attitude of the exchange banks in this respect. Thus it was pointed out by the Indian Merchants' Chamber, Bombay, before the *Indian Central Banking Enquiry Committee* that the exchange banks are literally forcing Indian exporters to insure their goods with foreign insurance companies. It was suggested that the Exchange Banks' Association should lay down standards to which the insurance companies should conform for obtaining the confidence of the exchange banks and that the Association should thereafter publish a list of Indian and Non-Indian insurance companies which conformed to these standards and whose policies should be accepted by all the exchange banks without limit. But even so lenient a proposal was not acceptable to the Exchange Banks' Association which evaded the issue by pointing out that the decision in the matter rested with each individual bank. Even to this day the situation has not improved and the foreign concerns have practically a monopoly in this line of business.

In recent years the number of Indian concerns carrying on business other than life is increasing. But the difficulties in their way are immense. It is quite natural that they will

have to face competition from their better-placed rivals. But if this competition is changed in favour of co-operation, immense good will be done to the business. For this purpose the newcomers as well as the old have certain duties. The newcomers should not accept unremunerative rates for attracting business. This does not always create good feeling among the parties even and makes the old concern lose their sympathy. A covetable ideal is better service. The bigger concern should see that the new ones get some business out of their excesses which are at present reinsured outside. The establishment of a Central Marine Claims Settlement Board may also be considered, at least for the smaller units for whom the maintenance of an independent arrangement would be too costly a luxury. The Board would help the standardisation of practice and procedure.

Market Research in Foreign Trade.

The most important, at the same time the most neglected, subject in India's foreign trade is market research. In these days of hard competition in world market, it is necessary to explore every possible facility for the expansion of markets. Besides, the more remote the market, and the more complicated the conditions, the greater will be the problem of sale. The regulations regarding foreign trade are not the same in different countries but vary and change from time to time. It is the function of the Market Research Committee to keep abreast of all these changes in law and usage. Besides, rapid changes are taking place in world market, in tastes and fashions and it is necessary that the producer should keep in touch with these changes. Sometimes the demand may be potential and can only be known as a result of research work. Sometimes, some foreign country may be carrying on research for finding out a substitute for a certain product, e.g., jute, and it is necessary to be informed beforehand so that adequate measures may be taken to secure competitive position. For these and thousand other reasons, market research has assumed importance particularly in foreign trade. In the large and highly developed export organisations in advanced commercial countries of the west, research work in foreign market

is constantly being carried on to some extent by a separate market research department. In the case of smaller concerns, it is not possible to maintain a separate research organisation. So they are sometimes found to maintain one common organisation, working for all.

The need for market research, as already hinted, is not much appreciated in this country. The history of the coal industry in India is a sufficient eye-opener. Before the first great war, India supplied coal not only to the Indian ports—both the Indian India and British India—but also to foreign ports like Colombo, Hongkong, Singapore, Aden and Durban. The Government of India had prohibited the export of coal from 1st September, 1920, but when the prohibition was removed and all facilities restored from 1st January, 1924, it was found that the foreign market had been lost. It must of course be admitted that India is not dependent on the foreign market for the sale of coal; but however small the export may be it is a disgrace to be ousted from foreign market. Therefore, a committee was appointed in order to investigate into the matter and on the basis of its recommendation the Coal Grading Board was organised in 1926. It is of course true that inspite of the efforts of the Board, shipments of cargo coal have been declining steadily in recent years, but as the *Coal Mining Committee* (1937) pointed out, "it is possible that the foreign trade would have disappeared altogether without grading."

Among other fields, mention may be made of two cases in which the government has taken some step for the exploration of market. One of these was the appointment of the Indian Trade Mission in 1928 in order to explore the possibilities of market expansion for Indian Cotton piecegoods. The Mission, as already pointed out, recommended the appointment of trade commissioners at three centres, but appointments were made at two places only, *viz.*, Alexandria and Mombasa. On the need for exploratory work, a well-known American authority on textiles, Kennedy, pointed out, in his *Profits and Losses in Textiles*, that the most significant factor to-day in the textile industry has been the economy of large scale merchandising and selling. A common co-ordinated policy for enlarging existing markets, the investigation of

new uses for cotton fabrics, the systematic exploration of export markets,—these are the numerous directions in which action is to be taken. As we have already seen elsewhere, the Trade Mission considered that an additional market for 80 to 90 million yards of cloth could be found in the territories covered by the Mission's Report, provided that a common selling organisation was brought into being; but the recommendation was not given effect to. In another field, the government, has helped to carry on market research. This was the appointment of the Meek-Gregory Committee to explore the possibilities of market for certain Indian products in America, which became necessary as a result of loss of market in Europe owing to the outbreak of the second world war. The possibilities explored were rather meagre.

Among the organisations instituted by the industry itself, mention may be made of two outstanding ones in this country, *viz.*, the Indian Central Cotton Committee and the Central Jute Committee. The functions of these bodies are varied and only a small part of their attention is given to research work of any sort, including exploration of markets. Thus one of the functions of the Central Cotton Committee is to carry on research in the plant breeding schemes for the improvement of quality. The Committee has also taken steps to bring to the notice of the trade, both in India and abroad, those improved varieties which have now reached a commercial scale. The functions of the Central Jute Committee include agricultural, technological and economic research, enquiries and recommendations relating to banking and transport facilities and transport routes, improvement of marketing in the interest of jute industry, collection and distribution of all relevant information on jute, etc. Be it noted however that the bearing of the above functions on the market research is only indirect. But there is no systematic organisation for the purpose. The merchants in the western coast of India going overseas, particularly to Africa, come into touch with final consumers in those regions and provide a sort of research agency as regards the tastes and demand of the inhabitants of these regions. In India, we find their prototype in the Chinese and Japanese hawkers moving inland and coming into contact with the ultimate consumer. That was one of the

reasons why Japanese goods, particularly cloth, found so wide a market in India. What these people have done in India should be taken as an example. The Interim Government in India has been showing interest in this respect and have sent Trade Missions to some countries. Similar visits have been organised by industrialists as well.

Trade Marks.

Trade marks are of very great importance in export trade in view of the fact that the customer recognises a particular commodity by the mark it bears. He has no direct connection with the producer; nor does he care to have any. He bears the mark in his mind and orders for it to his shopkeeper. It is for this reason that the manufacturer and the merchant dealing in it should make sure that the mark is not forged, and that this right is not infringed in any way in overseas market. For otherwise, the goodwill obtained by a particular make may be exploited by another firm producing the same line and adopting the same, or very similar, mark.

Three types of arrangements are to be found in the matter of trade mark. In the first place, the user of a particular trade mark obtains a right to the use of the mark, and when it is registered, it is *prima facie* evidence of the right already obtained by the user. This arrangement is to be found in some of the countries of the British Empire, minus India, some countries of Europe and the U. S. A. There is another group in which there is no sanctity about the use of a trade mark. As soon as a trade mark is registered, the persons who have been using the market for long without registration would be excluded from the privilege. The most important example of this type is Japan, as also some of the South American States. India fell in none of the above categories. Here there was no provision for registration of a trade mark but the principle recognised was that the person who first took a mark into use was entitled to it. Trade marks are to some extent protected in British India by Section 3 of the *Merchandise Marks Act* of 1889 and by the law of commercial goodwill. Under the former Act, the infringements or offences have been classified under four heads:—

- (a) Counterfeit trade marks;
- (b) Trade description false in respect of the country of origin;
- (c) Other false trade descriptions either in respect of their number, quantity, measure, gauge or weight, or in respect of the materials of which they are composed; and
- (d) Lengths not properly stamped on piecegoods.

The first non-official efforts at the restriction of the use of trade mark were made by the Madras and South Indian Chamber of Commerce and also the Bombay Mill-owners' Association. The former body used to register new trade marks on payment of a fee, though this registration conveyed no legal right. The Bombay Mill-owners' Association keeps a register of all trade marks in use by members and has a special set of rules governing their registration to which all members agree to conform, in view of the protection afforded by the Association to the trade marks and tickets used by them. The first legislation in this respect came into existence in 1940 when the Trade Marks Act, was passed which provided for the registration and more effective protection of trade marks. The definition of trade marks in law is not the same but varies in different countries. The U. K. Trade Marks Amendment Act of 1937 gives the following definition: "A trade mark shall mean . . . a mark used or proposed to be used in relation to goods for the purpose of indicating, or so as to indicate, a connection in the course of trade between the goods and some person having the right either as proprietor or as registered user to use the mark, whether with or without any indication of the identity of that person. . ." In the newly enacted Indian Law, a "mark" includes a device, brand, heading, label, ticket, name, signature, word, letter or numeral or any combination thereof, and a trade mark is a mark used or proposed to be used in relation to goods for the purpose of indicating a connection in the course of trade between the goods and some person having the right to use the mark. Thus it is clear that the definition of trade mark in both the

is almost the same. Two types of registered trade marks are to be found. In the first type, which is most common, registered trade mark contains either the name of the company, individual or firm represented in a special or particular manner, or the signature of the applicant for registration or some predecessor in his business, an invented word or words, a word or words having no direct reference to the character or quality of the goods, or any other distinctive mark. In the second type, the mark applied for should be capable of distinguishing goods with which the proprietor of the mark is or may be connected in the course of trade from goods with which he is not so connected. The latter type is to be found in New Zealand and some parts of Africa.

In most of the countries, before a trade mark is accepted for registration, it is compared with marks which are there already on the register and if it is found that the mark resembles any other mark already inserted so as to create confusion it is refused registration. In the Indian law, trade marks contrary to law or morality or dis-entitled to protection in a court of law by virtue of their being likely to lead to deception or confusion, shall not be registered. Further, applications for registration of trade mark are liable to be opposed and the decision of the Registrar will be appealable to the High Court having jurisdiction. Original registration will be in force for a period of seven years and may be extended by another 15 years at a time.

Another interesting provision of the Indian Act is that any person, not being a trader in the goods in question, who undertakes to certify the quality, standard, purity, or some other characteristic of any goods, may register a trade mark as a certification trade mark, on approval from Central Government. The Act also contains provisions for the defensive registration of trade marks and for registering "permitted use" of the trade mark by other persons than the proprietors of such marks.

Registration of a mark, be it noted, gives the right to the exclusive use of the mark as it is registered; but it does not of necessity give exclusive right to every feature of the mark. If the label only or the word or figure or any distinctive mark therein be registered, the unregistered part may con-

veniently be used by any other competitor. Thus if label alone is registered, the mark or word therein may be copied on a slightly different label; and if the mark or word alone is registered, a slightly different word or mark may be used on a similar label. It is wise therefore to have each and every part of the mark and label separately registered, so that there may not be any scope for confusion or litigation.

Government Departments connected with Foreign Trade.

The following departments of the Government of India are connected with the foreign trade of the country:—

Department of Commercial Intelligence and Statistics.

We have already mentioned this department and noted some of its functions. Apart from the functions already mentioned, it advises the Government of India with regard to the fixation of tariff valuations for the purpose of customs duties levied in India. It is also concerned with the publication of *Indian Trade Journal* and the *Annual Review of Trade* and various other matters relating to Indian trade. A new section known as the *Statistical Research Branch* has been subsequently established for doing research work on economic problems in which the Government of India are interested and to carry out a continuous analysis and interpretation of economic and statistical facts and phenomena for a proper appreciation of the economic situation in the country and this branch is also responsible for the publication of the *Monthly Survey of Business conditions* in this country.

Patent Office.

The law and procedure in India for the protection of inventions and registration of designs closely followed that in the U. K., the only important difference being that in the absence of any legal provision for the registration of trade marks, India could not be a party to International Convention for the protection of industrial property, under which certain

rights of priority are obtainable in other countries. The reciprocal arrangement with the U. K. and the Dominions afforded, however, a partial substitute. With the passing of the Indian Trade Marks Act of 1940 the situation, it is expected, would improve when the whole of the Act comes into operation. One important Section of the Act, *viz.*, Section 85 has already come into force. It authorises the Central Government to prescribe the necessary procedure for the deposit of trade marks at the Patent Office in advance of the coming into force of the remaining provisions of the Act.

Customs Department.

It is controlled by the Central Board of Revenue which is attached to the Finance Department of the Government of India.

Indian Stores Department.

The story of the Indian Stores Department and that of the stores purchase policy of the Government of India make an interesting reading and is revealing of the step-motherly treatment accorded by the Government to the producers in this country. It is well-known that the various departments of the Government and the Railways in India purchase immense quantities of stores of all kinds. The stores purchase policy of the Government and of the Railways is a matter of history: suffice it to say here that when the *Industrial Commission* was carrying on its investigations the Government policy in this respect was anti-national in character and although the Government tried to justify their policy, it was pointed out by the *Industrial Commission* that it was possible to regulate the stores purchase policy in such a manner as to stimulate Indian industries. The Commission went further and pointed out certain improvements in the methods of purchase, which if adopted, would not only be to the benefit of existing industries but lead to the establishment of newer lines of production in this country. For long even after the recommendations of the

Commission had come out, no action was taken. At long last, in 1922 the Indian Stores Department was constituted. Its main function is to purchase in India and abroad, in accordance with the Stores Purchase Rules, stores of all descriptions except lethal munitions, foodstuffs, medical stores, stationery and a few other classes of articles, for the Departments of the Central Government and the minor Local Administrations and to inspect stores purchased by the Department or by the consuming departments direct. Its services are also available to such major local Governments, Indian States, public bodies, etc., as may desire to avail themselves of these services. The purchase activities of the Department are not confined to Indian markets. Orders for stores not obtainable in India are placed abroad in accordance with the Stores Purchase Rules. The Indian Stores Department and the Indian Stores Department, London, are at present entirely distinct organisations and function independently of each other, but the services of the London Stores Department are freely utilised by the Indian Stores Department for the inspection of stores purchased abroad.

Entrepot Trade of India.

The favourable position of India in the Eastern hemisphere had been the main reason for the development of entrepot trade even in early times, Indian ports working as a link between the East and the West. In recent times also India had maintained the tradition. But after the first great war, the entrepot trade recorded a decline. The principal reason for this is that countries depending on India as entrepot are all gradually developing direct trade relations with the country of export. The shares of the principal countries in the total entrepot trade of India in 1940-41 were as follows:—The U. K. 2 p.c.; the U. S. A. 51 p.c.; Burma 16 p.c.; Arabia and Iraq 4 p.c. each and Ceylon and Egypt 3 p.c. each. The bulk of the trade in that year passed through Sind which accounted for 49 p.c., while Bombay had 34 p.c. and Bengal 16 p.c. The following table gives the value of the principal articles re-exported, arranged in the order of their importance:

(Source: *Review of Trade of India 1940/41*).

Value in thousands of Rupees.

		1909-10 to 1913-14 average	1914-15 to 1918-19 average	1919-20 to 1923-24 average	1938-39	1939-40	1940-41
Hides & Skins, raw			287	5,065	21,913	45,055	51,684
Cotton, raw		14	66	6,654	1,558	1,309	1,453
Cotton, manu- factures—							
Piecegoods	{ Grey	840	7,927	19,539	1,543	1,091	3,891
	{ White	1,714	4,688	4,958	592	558	1,305
	{ Coloured	11,679	13,619	11,229	873	1,617	4,029
	{ Twist & Yarn	805	1,277	2,047	1,233	496	671
Other Sorts		713	1,819	2,160	234	250	418
Total		15,765	29,396	46,587	6,033	5,321	11,767
Wool, raw		4,250	10,206	9,803	3,126	5,799	7,900
Wool, manu- factures		416	837	5,763	1,239	1,288	1,157
Total		4,666	11,043	15,566	4,365	7,087	9,057
Machinery & Mill-work		568	489	1,642	1,796	1,736	3,200
Hardware		1,389	1,183	2,708	2,445	2,026	2,089
Sugar ...		5,295	11,257	31,623	10	5,546	1,620
Silk—							
Raw ...		123	200	498	35	84	204
Manufactures—							
Piecegoods		637	1,167	1,498	938	797	517
Other sorts		66	241	394	810	629	477
Total		826	1,608	2,390	1,783	1,510	1,198

	1909-10 to 1913-14 average	1914-15 to 1918-19 average	1919-20 to 1923-24 average	1938-39	1939-40	1940-41
Fruits & Vegetables	1,311	4,223	5,365	1,137	907	943
Rubber Manu- factures	112	90	381	339	324	418
Gums and resins	1,054	1,359	2,304	435	476	408
Haberdashery and millinery	—	395	812	535	389	285
Apparel (exclud- ing hosiery, boots and shoes)	1,589	1,389	4,822	938	590	264
Postal articles	1,624	2,385	4,516	157	153	150
Total value of Re-exports	46,188	81,438	1,56,474	64,236	96,532	1,18,128

Appendix on Geneva Tariff Negotiations.

The recent political changes in India have introduced a lot of change in foreign trade matters. Henceforth everything will be determined not by political factors but by economic considerations. Even the future of Imperial Preference is not sure. The recent Conference on International Trade and Employment which met at Geneva has resulted in a reduction in Imperial Preference to which the British Commonwealth has agreed. By the terms of the *23-Nation Geneva Trade Agreement*, the British Commonwealth has agreed to the elimination of Imperial Preferences on 5 p.c. of their 1938 value and reductions in preferences amounting to a further 25 p.c. Commonwealth countries have agreed to reduce duty rates on U. K. goods to the extent of £12 million of their 1938 value and to limit to the present rates duties on a further £15 million worth of goods. 89 p.c. of the South African preferences and 64 p.c. of those of India and Pakistan have how-

ever been maintained. Under the Agreement, China has granted tariff concessions covering British trade valued at £2 million in 1938. The U. S. A. has agreed to halve duties on the U. K. exports worth £2½ millions in 1939 and to reduce by one-third and one-half the duties on other exports worth between £10 millions and £11 millions. Thus the gain of Britain from "binding" and reduction of duty amounts to £29 million according to 1938 value. On the other hand, Britain has agreed to bind duty-free entry or *advalorem* duties at current rates on goods, the imports of which from foreign countries concerned amounted to £63.1 million in 1938 and to reduce rates on goods the imports of which were valued at £30.4 million in 1938. This is an entirely new experiment full of significances for the future, though, of course, "concessions on individual margins of preference do not by any means involve an abandonment of the essential structure" of the system of preference. And yet the gains for Britain are considerable. For, while the reduction in preference is small (70 p.c. being unaffected, 5 p.c. only eliminated, 10 p.c. reduced by 35 p.c. or more and 15 p.c. reduced by less than 35 p.c.), the gains from the reduction of protective duties by other countries are considerable. Thus from China alone, Britain has obtained concessions to the extent of trade valued in 1938 at £2 million. Concessions have been obtained in the case of sheep's wool, iron and steel plates, tyres, proprietary medicines, steam boilers, electric dynamos, embroidery, linen and textile machinery. Export trade, as is well-known, is the lifeline of British economy and no other country stands to gain as Britain from this "revival of multilateral trading conditions and the outlawing of protective restrictions."

India is a participant in this trade agreement. It is estimated that as a result of tariff negotiations, India will be able to reap advantages to the extent of Rs. 35 crores as against those worth Rs. 31 crores which she will have to give. Besides, she will reap an indirect advantage to the extent of Rs. 13 crores. The above negotiations have been conducted with 15 countries, from which South Africa, U. K., Ceylon and Burma are excluded. No negotiations were opened up with South Africa, because for the time being all commercial transactions between the two countries have been suspended. The

trade relations between India on the one hand and the U. K. and Ceylon on the other are sufficiently covered by the Indo-British Trade Agreement of 1939. The reasons for not negotiating an agreement with Burma were also similar. Since the change in political status has given India the freedom of action in economic matters, in conducting these agreements, three principles were kept in view, *viz.*, first, concessions should be such as are demonstrably in the interests of national economy or not injurious to national economy; second, concessions should not relate to products which are protected, or in respect of which a claim to protection is likely to be made during the next three years; and third, concessions should not result in any excessive loss of revenue. It should be remembered that, in earlier trade agreements, noted earlier, India has every time suffered injustice, there being no consideration of the backwardness of the Indian economy and of the needs of such an economy. Even now, as the matters stand at present, India will not be able to reap the full benefits of these agreements unless she develops her internal economy by progressive industrialisation and also her export trade.

The Geneva Tariff Negotiations aimed at a substantial reduction of tariffs and other charges on exports and imports as also at the reduction or total elimination of preferences on reciprocal basis. For the sake of convenience, in a large number of cases, negotiations have been conducted "on a bilateral and selective product-by-product basis, and the concessions took the form of (i) reductions in customs duties or other import charges; (ii) reductions or elimination of preferential margins; and (iii) binding of existing tariffs against increase. In view of the multilateral character of the agreement, however, the benefits of these negotiations will even independently of the existence of any most-favoured-nation-treatment agreements be generalised in favour of all contracting parties." This reduction of tariff and elimination of bilateral trade are expected to pave the way for multilateral agreements. The only fear may come from U. S. A. but even she has agreed to reduce her tariffs on a range of goods thereby enabling the nations to get dollars, the supply of which is much shorter in proportion to demand. These agreements at tariff reduction have however made one concession, *viz.*, that

the devastated European economies will still be able to enforce quantitative restrictions on imports from the U. S. A. till 1952, thereby being able to protect themselves from an inflow of non-essential imports. Similar exception should have been made even in case of backward economies.

These agreements indicate a good start and if allowed to function satisfactorily they will prove to be "very substantial contribution towards cutting the shackles hampering international trade." If these work properly, 23 nations will reap benefit from them. But there are so many obstacles. First, these depend on how the European countries are settled on a peace basis and second, these depend on the successful development of the internal economies of the backward countries and their increasing participation in foreign trade. Only these matters will decide whether the world is going to see a free flow of international trade or whether it is receding to restrictionism and more restrictionism.

PART III
ASPECTS OF FINANCE.

CHAPTER IX

Need for Producers' Finance and allied Problems.

The discussion on aspects of Finance naturally falls into two parts, Producers' Finance and Distributors' Finance. As in the case of organisation, so in that of Finance, these two are quite distinct, but equally important. It is the purpose of the present part to give attention to this aspect. First we shall consider the Producers' Finance in its various aspects and then take up Distributors' Finance. One question is often mistaken in the discussion of Finance. It is this that the requirements of Finance are not the same in different stages of industrial development for different countries. Often a case is made for instituting some organisation for supplying the financial requirements of industries in this country on the ground that similar needs arose in Europe after the first great war and was adequately responded to. But in these matters, as in many others, to draw a parallel is to do a mistake. The need for industrial finance in this country is old, going back to the days of the great turmoil of the decline or fall of the Mughal Empire and the rise of foreign rule in this country. But the need was not met, nor even felt by the administration. The indigenous agencies had declined or had been crippled owing to the influx of the Western influence. Thus a gap was created in the field of finance, never to be fulfilled by any systematic body of organisation even to this day.

The need for finance felt in India after the first great war was not the same in character as the need felt in Europe. Europe had passed through four years of war and destruction. During these years, there was scientific revolution in some countries but not in all. Therefore Europe's problem was one of reorganisation, reconstruction and modernisation. Not so in India. We had first half a dose or even a spoonful of

industrial development, a drop in the ocean, when compared with the immense resources, both material and human, during the four years of war. But more important than that was that the war was a great instructor in so far as it brought home the need for industrial development. In matters of supply of the essential requirements, dependence on a foreign country, particularly when the trade is dislocated owing to the outbreak of hostilities, is a curse. The need was therefore felt. But this can only be fulfilled by a positive policy on the part of the administration. What that policy had been and how far it has benefited the industries is not a part of the present discussion; suffice it to say that "a quarter of a century divided the present war from the last, but India remained nearly as unprepared as before to face the inevitable difficulties arising out of the war or to exploit fully the industrial opportunities it afforded." But whatever that may be, the fact remains that the need for finance is one for construction in the main.

The initial requirements of capital are of two types—short-term and long-term. The supply of short-term capital has not met with much difficulty. But long-term finance is the problem of Indian industry. Much discussion has taken place on the problem and numerous suggestions have come forward. In the present work we are not concerned with these paper discussions but shall consider how Indian industries are actually financed, along with their capital structure. One thing must however be remembered. ✓The system of financing an industry is important from two points of view. ✓In the first place, the system of finance should be such as not to impose any unnecessary burden. In these days when competition, however imperfect, is not only intranational but international as well, economy in every possible aspect should be the goal. But if, owing to an unscientific system of finance, an unnecessary burden is imposed on the industry, it stands in the way of its development. ✓And secondly, progress demands that there should not be any obstacle in the way of the industry. Nobody knows at what unforeseen and unforeseeable moment some chance may come; and unless the industry is strong financially it cannot avail of it and may therefore deteriorate in competitive position. In the same way in order to face depression also, the industry must be financially strong. In

fact, the need for strong financial position is even greater in the years of depression than in those of prosperity. Our experience in this country has been that as soon as depression has overtaken an industry, the sources of finance, meagre in normal times, are altogether blocked, leaving the industry in a helpless state of affairs. Thus, for instance, many industrial concerns in this country would have collapsed during the last world depression owing to the silting up of the financial stream but were somehow maintained by the managing agents who are known for financial integrity.

What is the sound method of financing industries? It is, of course, difficult to lay down hard and fast rules. But it is well-known that there are three possible sources—floatation of shares, borrowing money on short-term or long-term, and corporate saving, as distinguished from the former two, which mostly, excepting in case of subsidiary company, are the result of individual saving. When a new industry is to be floated, the last source is of no avail in view of the fact that accumulation of reserve takes time. In that case, a sound financial policy demands that the burden imposed thereby should be the least. Thus the concern should at first strive to raise as much capital by the floatation of ordinary shares, with least possible or no obligation at all, as the circumstances permit and only when this source is exhausted that resort should be had to borrowing. For, when the capital liabilities of a concern include a huge proportion of shares, bonds and debentures can be sold in the market at a higher price than when the capital structure of a concern is over-burdened with debts and financial obligations of other sort. For, “a company without debt is a company that is solvent and solvency is the principal thing. Modern industry, no matter how well-protected by supposed monopolistic advantages, is subject to such revolutionary changes in methods and markets that the introduction of fixed interest obligations, which carry sinking funds as well,—another form of fixed charge—should, if possible, and in the absence of weighty advantages in the contrary policy, be avoided.” (Mead, *Corporation Finance*.) In India, however, the same argument does not apply in all cases. There are certain instances in which not only adequate and certain attraction have to be provided for, but also the repayment is

to be assured. This is particularly a feature of the Railways in this country which we shall consider later. So far as sound financing goes, it must be admitted that the lesser the burden, the greater the progress.

When the industry has developed to some extent, conservatism demands that the financial needs should be met from corporate saving, thereby reducing the dependence of the industry on outside sources. Corporate saving not only facilitates industrial finance, but adds to the prosperity of the industry. It facilitates expansion in the same or allied lines, stabilises the rate of dividend and adds to the prosperity of the shareholders. We shall consider this aspect of the problem later where it will be seen that it has not assumed much importance in many industries of this country, some of which, though declaring fat dividends, do not always realise the necessity of maintaining reserve. So far as the banking companies are concerned, there is the legal provision and in their case corporate saving is a matter of compulsion. There are industrial concerns, like the Tata Iron and Steel Works, which maintain sufficient reserve and invest it in the industry itself, which has been questioned by some but justified by others. And there are still others, like the tea industry where the companies declare fat dividends but do not seem to be alive to the question of maintaining reserve. These will be considered in their proper place. But the principle may be laid down that each concern should, in its own interest, adopt a conservative dividend policy and transfer a portion of undistributed profits to the reserve. It is often found that concerns declare dividend, high or low, according to the profits of the year. But this tells unfavourably on the price of securities in the market. If the concern adopts a conservative policy, it can maintain not only the rate of dividend but also the price of securities, and add the surplus profits to the reserve fund.

To-day we have reached a stage in which the problem of finance has assumed greater importance. Everywhere we hear of planning and planning of some sort must come if we are to survive economically. But planning requires finance. Whatever the nature of the plan may be, whether industrial or agricultural, whether capitalistic or communistic, capital is the essential factor, capital not merely in the sense of money

capital but also material capital, without which no plan can go on. Planning is needed not for its own sake, but for the greater interest of the community and must be comprehensive in character. The greatest defect of the paper plans formulated in this country is that they are partial, piecemeal and therefore bound to fail. But that is a different question; taking it for granted that a system of planning is introduced in this country which is beneficial to the greater interest of the country, the next problem is one of getting finance.

Here arises the question of saving and investment. For any country, saving is the most important source of finance, though for most countries, it is not the only source. Taking the case of India, it can be seen that in investment, saving has played a comparatively smaller role, say, before the first great war, and the inflow of foreign capital had been the main source. India is not a solitary figure in the list of this type of countries; there are many who depend on foreign capital in investment matters. Therefore the Keynesian assumption that savings of necessity equal investment, though true for his own country, is absolutely falsified for others, where saving is a microscopic proportion and the country is dependent on foreign sources. Even in case of England, saving cannot be equal to investment unless this investment includes investment in overseas colonies, dependencies, etc. Whatever that may be, it may be said here that with the growth of national income of a country, the savings increase, possibly more than proportionately, after a certain stage in the uplift of the standard of living, to the increase in national income. For, the greater the income, the less the consumption and therefore the gap between individual income and consumption, and so also between national income and consumption, increases, thereby increasing the savings of the nation. This conclusion however is not always true and it will be seen in the following table that the percentage of national income saved, instead of increasing, has decreased in case of some countries:

(Source: Clark: *Conditions of Economic Progress*.)

Upper Line—Income per head of working population on 48-hour work basis, International Units.

Lower Line—Percentage saved.

	1900-10	1913	1919-24	1925-30	1934-37
Great Britain	{ 926	—	1117	1208	1323
	{ 12.2	—	8.1	7.6	7.0
U. S. A.	{ 1325	—	1499	1672	2013
	{ 14.3	—	12.2	10.9	5.0
France	{ 630	629	—	681	—
	{ 9.0	12.5	—	11.2	—
Germany	{ 670	—	—	722	864
	{ 19.1	—	—	7.7	11.8
Russia	{ 330	342	—	325	358
	{ 8.2	9.0	—	7.8	14.2
Japan	{ —	—	195	312	362
	{ —	—	21.9	19.8	21.9

This justified our use of the word 'possibly' above. For the assumption that savings increase, though not proportionately with increase in income is not true even in England, where with 926 I. U. of income per head, the percentage of income saved was 12.2, but with the increase in national income to 1323, the savings per head declined to 7.0. Any hard and fast rule is therefore difficult to lay down where psychological considerations predominate over economic ones. So far as India is concerned, no such precise statistics have been compiled. But in the opinion of the Bombay Planners, who can legitimately claim a considerable touch with the economic development of the country, "we do not assume that more than 6 p.c. of the national income on an average would become available for investment during the period of the plan. On this basis the total amount which should be obtained over the whole period from the savings of the people would be in the neighbourhood of Rs. 4,000 crores," or Rs. 266 $\frac{2}{3}$ crores per year. This estimate of the national saving of India is much higher than those made previously which have often varied between Rs. 75 to Rs. 100 crores per year, and may or may not materialise according as the plan is successfully introduced or not.

But saving is one thing and investment another, and the latter may exceed or fall short of the former as the circumstances demand. When national savings, both individual and corporate, are not enough, resort must be had to other sources, within the country or without. One such internal source is inflation, rather deflation. If wartime requirements, with destruction as its objective, can lead to inflation without the confidence of the people in the currency being shaken, why should the peacetime constructive purposes be left uncared for for want of money? New money injected in the system will not only lead to expansion of the economy but maintain the atmosphere of prosperity created during the years of war. "There is nothing unsound in creating this money because it is meant to increase the productive capacity of the nation and in the long run is of a self-liquidating character." The Bombay Planners are not blind to the possible troubles of created money from which the economy may have to suffer and to the gap that may arise between the volume of purchasing power in the hands of the masses and the volume of goods made available. But then "in order to prevent the inequitable distribution of the burden between different classes which this method of financing will involve, practically every aspect of economic life will have to be so vigorously controlled by Government that individual liberty and freedom of enterprise will suffer a temporary eclipse."

So far as external source of finance is concerned, we have at present three avenues, sterling securities, balance of trade and payment and foreign loans. The nature and amount of the first source are well-known; the main problem is one of utilisation of these balances. We have already seen how India's hands are bound as regards their liquidation and possibly also as regards the nature of purchases when India is free to do so. As regards the second source, we have already expressed pessimism, in view of the fact that the excess of exports from India over imports will be absorbed in meeting some of the obligations which though not necessary are yet permanent in character. If however the Government pursues an enlightened policy, makes provision so as to provide for India's own bankings, shipping and insurance services, and determines the ratio at rates already suggested,

some help may be obtained from a favourable balance of trade and the export surplus may be converted into imports of necessary capital goods. But the change in policy suggested seems to be too revolutionary to obtain the approval of the Government in its present form. Whatever that may be, the Bombay Planners have pinned their faith on these sources. Thus the amount of capital which they expect to get from these various sources are as follows:

External Finance—	(Rs. in Crores)
Hoarded Wealth	... 300
Sterling Securities	... 1,000
Balance of Trade	... 600
Foreign Borrowings	... 700
	2,600
Internal Finance—	
Savings	... 4,000
Created Money	... 3,400
	7,400
Total	10,000

The need for finance is indicated in the above table. For the post-war economic planning which, in the Bombay Plan, is predominantly industrial, a sum of Rs. 10,000 crores will be needed over a period of 15 years. But this does not exhaust the need for producer's finance in this country. What we want in future is not an agricultural economy alone or an industrial economy alone, but a balanced economy in which both agriculture and industry will be developed equally. For by this time we have become familiar with the evils of a non-balanced economy in war and peace, and if stable economic progress is to be maintained, agriculture must be no less developed than industry. This also will present the need for producer's finance.

In this chapter we have indicated the need for producer's

finance in different aspects. It is now for the planners to investigate the different sources from which it may be availed. In the following chapters we shall devote ourselves, as students of business organisation, to the existing system of corporation finance in this country.

CHAPTER TEN

CORPORATION FINANCE IN INDIA.

Existing Financing Agencies.

In the Corporation Finance in India, there are five principal sources. They are: managing agents, banks, public deposits, share capital and debentures issued. We do not have any comprehensive statistics regarding the comparative importance of these different sources for the whole country. The following table, however, gives some idea regarding the situation in Bombay and Ahmedabad:

(Source: *Indian Central Banking Enquiry Committee, Minority Report.*)

	Bombay (Figures for 64 mills)		Ahmedabad (Figures for 56 mills.)	
	Lakhs of Rs.	Percentage of total finance.	Lakhs of Rs.	Percentage of total finance.
Amount loaned by the Managing Agents	532	21	264	24
Amount loaned by banks	226	9	42	4
Amount of public deposits	273	11	462	39 ✓
Amount of share capital	1,214	49	340	32
Amount of debentures issued	238	10	8	1

It will be seen from the above table that about 50 p.c. of the total finance in Bombay is raised by the floatation of shares, while public deposits are more important in Ahmedabad. In both the cases, managing agents account for about one-fourth

of the total capital, while the place occupied by banks is negligible. We shall consider in brief the services rendered by these different agencies with regard to corporation finance.

Managing Agency System.

The managing agency system was the result of gradual evolution and originated out of the lack of any suitable agency for providing industrial finance. The joint stock type of business organisation being new to this country and owing to the lack of organised financial institutions, the managing agency system came to play the role of industrial promoters and financiers. It is interesting that it was introduced first in Bengal by British merchants and was adopted later in the west coast of India by Indian merchants, particularly Bhatias and Parsis. But the functions of company promoters of the western countries are not of the same type as those of the managing agents. For, the function of the promoters ceases as soon as the promotion business proper is over; but the function of the managing agents is more or less of a permanent nature and their interests become identified with those of the company.

The legal provision also encouraged the formation of managing agency concerns. Upto 1913 no elected Board of Directors was required for a joint stock company compulsorily; and even after that, upto 1936, the directors were the creation of the managing agents, and hence regarded as anomaly in some quarters. But the requirement of law was there and had to be fulfilled and therefore the directors were taken from among those who were most often friends or business associates of the managing agents.

The managing agency concerns were started either as family concerns which later on were converted into partnership or were partnerships from the very beginning. In Ahmedabad, and in some instances, in Bombay, the managing agency is a family concern, being hereditary in character and permanent in tenure. The managing agency system in Calcutta originated mainly as partnership, the number of partners sometimes exceeding a dozen in number. It is natural that when the partnership firm, consisting of a large number of partners, manages a concern, only a limited proportion of the shares is

available to the public for subscription. Where the system has remained hereditary in character, there is no scope for the infusion of new blood; but where it originated as partnership or was later converted into it, it has maintained original efficiency. For new partners are not always taken from the relatives of the retiring partners, but from, say, the senior assistants, who have acquired a lot of experience by constant association. Even when some relative of the retiring partner is taken, he is not made immediately a partner, but is given a lower rank and if he proves fit in time, he is made partner as soon as a vacancy arises. Obviously this system cannot suffer in efficiency.

When a managing agency concern starts business as partnership, the partners agree to take a certain proportion of the shares, and usually the minimum number of shares taken by the agency firm is 25 p.c. of the shares of the mill company. In Ahmedabad, however, where family business predominates, the organisation of the managing agency concern is different. *The Indian Central Banking Enquiry Committee* gave the following description of its organisation and functioning: Generally speaking, the total block capital required for starting a cotton mill in Ahmedabad is about Rs. 20 lakhs and of this Rs. 5 lakhs is initially found by share capital. As regards the balance in case of old mills, 65 to 75 p.c. of the capital outlay has been financed by deposits and by funds supplied by managing agents. In case of new mills, deposits are no doubt encouraged, if necessary, by the grant of a share in the commission of the managing agent; but the managing agency is made into a limited concern with a nominal capital of Rs. 1,000, there being 1000 shares of Re. 1/- each and any one who comes forward with Rs. 5,000/- i.e., Rs. 3,000 in the shape of ordinary share capital and Rs. 2,000/- in the shape of deposits for a fixed period of seven years is given one share of the managing agency or one-thousandth share of the agency commission. This one-rupee share has considerably more value than its nominal value and in some cases it is worth Rs. 700 to Rs. 800. Formerly the managing agents used to take in persons who would bring in a certain amount of capital, thereby earning a certain portion of the commission agent's share, but now the agencies have been made into limited con-

cerns and shares issued, a proportion of which the holders may sell off at their discretion. Thus the members of the public do not come in as direct holders of shares, but get them through the managing agents, the result being that while the managing agents get their commission on the total holdings in their names, the real owners of share are only entitled to dividend, if, and when, declared. The partnership agreement is virtually non-terminable; but if a partner wants to transfer his rights, the other partners are given the first chance to purchase his portion. Even where agreements are terminable, adequate care is taken to see that the managing agents are not easily turned out.

Some of the above defects have been sought to be removed by the *Indian Companies Amendment Act, 1936*. Under this Act, appointment of managing agent is not valid unless approved by the company in general meeting. The managing agent is appointed under an agreement with the company and his powers are defined by such agreement. At first sight, it seems that the provision is quite far-reaching; but actually it is not. For, the managing agent is not merely the financier after a company is promoted, but is also the promoter. This being so, it is unlikely that the shareholders can throw out the managing agents after the concern is promoted. The importance of the managing agent is felt at every stage. Another provision of the Act is that the managing agent cannot hold office for more than 20 years at a time. Even managing agents appointed before the commencement of the Act of 1936 shall have to vacate office after the lapse of 20 years from the date of commencement of the Act, i.e., on 15th January, 1937, unless then reappointed. The provision for re-appointment is quite sound in view of the fact that continuity in administration is beneficial to the concern itself, unless, of course, there is any serious reason for their removal.

Whatever the defects of the managing agency system, its importance is felt at every stage. In a country where industrial promoters are conspicuous by their absence, the managing agents have played the role of company promoters. The function of promoting a concern begins with the conception of an idea which serves as the foundation of business. From the time the idea takes its origin to that when it is translated into

reality and the corporation starts functioning and exploiting the idea, the whole process is collectively known as promotion. In this country to whatever important industry we turn, jute, cotton, tea, sugar, electric supply and light railways, the achievement of the managing agents is quite apparent. Even the idea regarding the present Tata Iron and Steel industry and hydro-electric industry originated in the brain of the late Sir Jamshedji and was brought into practice through the managing agency of Tata Sons, Ltd. But unlike that of the company promoters of the West, the function of the managing agents is not restricted to promotion only, but includes in its scope the provision of finance, not only for initial fixed capital expenditure and for working capital, but also for subsequent re-organisation, extension and modernisation. They provide this finance in various forms—by subscribing shares and debentures themselves and arranging for their subscription by their friends, relatives, and even the public, in view of the attraction of the great name of a managing agent being associated with a concern, by arranging loans from banks on their own security, by attracting deposits from the public, and even making advances from their own pocket. In a country where under capitalisation is almost universal, its evil effects have been obviated by the existence of the managing agency system. In Ahmedabad, it was pointed out by the Mill-owners' Association before the Tariff Board of 1932, that in individual cases about 85 to 95 p.c. of the shares were held by the managing agency. Although in Bombay, the managing agency did not hold so large a proportion of shares, yet their holding was by no means negligible, unlike in Bengal, where with a few minor exceptions, the share holdings of a company by the managing agency scarcely exceed 25 p.c. and have at times gone so low as 5 p.c. This difference in the holdings in Bombay and Ahmedabad on the one hand and Bengal on the other is due to difference in business practice. For the managing agency firms, particularly the European ones, work more as underwriters than as financiers, their object always being to pass over as many shares as possible to the members of the public. Even when they are not so passed over, it is found that the shares are not held in the name of the company, but in that of different partners or their relatives and

associates. The tradition in this part of the country is not to hold the maximum number of shares but distribute them among the public and the less the holding of shares by managing agents, the greater is their success, for they deem it a matter of pride that the public have confidence in them and have taken over the shares of concerns under their managing agency. This too much holding of shares by managing agents in Bombay had its evil consequences in the years of depression following the first great war when most of these shares were disgorged on the stock exchange leading to too much speculation and ruin of many innocent investors.

Besides being the most important single shareholder or underwriter, the managing agents work also as creditor of a concern by taking up debentures. It is well-known that debentures as a form of investment is not very popular in this country, nor are they popular with banks and insurance companies. The managing agents have filled up an important gap in this respect as well. But apart from this direct financial assistance, both as proprietors and creditors, they have another, an indirect role to play: for public deposits and bank credit depend not so much on the credit of the concern but on that of the managing agency firm under whose agency the concern works. Bank credit however plays a minor role in Bombay and still less in Ahmedabad; but the fact remains that whatever financial assistance has been secured is due to the managing agents. In Calcutta, public deposits are not a source of finance and therefore the dependence on bank credit is considerable when compared with Bombay and Ahmedabad; but this requires the personal guarantee by the managing agents that the bank credit granted and availed of is always covered by stocks. This is not all. In some industries, as in tea and electricity supply, which take time to stand on their own legs and show profits, the financial backing of the managing agents is often required in the years following the establishment of the company. In the years of depression also, managing agents stand by the concerns under them. For, they have a high sense of self-respect, to preserve which they are ready to stake their all, a feature which possibly is peculiar to Indian business only. "Had not the managing agents retrieved the companies by their steady and persistent

nursing at considerable sacrifice through all the barren years of their existence, they would have been forced into liquidation, many a valuable industry would have been lost to the country and the shareholders would have lost their all."

In return for the services rendered, the managing agents receive some remuneration. The three forms of remuneration as described by the Tariff Board on Cotton Textile (1927) are as follows:—

"1. The system of remuneration by commission on profits which, since profits increased so largely during the war period, has been the most common system in Bombay and in most upcountry centres where it was, we believe, first adopted in 1888. The commission in Bombay ranges from $7\frac{1}{2}$ p.c. to $12\frac{1}{2}$ p.c., but in the majority of cases, it is 10 p.c. and the managing agency agreement usually provides for a minimum commission.

"2. The system of commission on production which is still in force in a few mills in Bombay and Ahmedabad but is more common in upcountry centres. The usual rate of commission is 3 pies per pound. In most cases provision is made in managing agents' agreements for the relinquishment of a portion of the commission according to the percentage of the dividend distributed.

"3. The system of commission on sales which is the most common system in Ahmedabad where it was introduced in 1895. It practically completely replaced the system of commission on production in 1917 when the era of high prices set in. It is also in force in three mills in Bombay and in several mills in upcountry centres. The rate of commission is usually $3\frac{1}{2}$ p.c. In this case also, provision is made in the managing agents' agreement for a relinquishment of a portion of the commission."

Since the passing of the *Indian Companies Amendment Act* of 1936, the basis to be adopted for the determination of the managing agents' remuneration has been specifically mentioned. Thus after the commencement of the Act, "the remuneration of the managing agent shall be a sum based on a fixed percentage of the net annual profits," the net annual profits of the company being "the profit of the company after allowing for all the usual working charges, interest on loans

and advances, repairs and outgoings, depreciation, bounties or subsidies received from any government or any public body, profits by way of premium on shares sold, profits on sale proceeds of forfeited shares or profits from the sale of the whole or part of the undertaking of the company but without any deduction in respect of income-tax or super tax or any other tax or duty on income or revenue or for expenditure by way of interest on debentures or otherwise on capital account or an account of any sum which may be set aside in each year out of the profits for reserve or any other special fund," and also an office allowance as fixed by the contract of management. Any remuneration over and above this should be sanctioned by special resolution of the company. But it must be remembered that these provisions apply only to fresh agreements; therefore, all the above methods of determining remuneration are in use. We have already seen that the system of paying commission on profits is popular in Bombay, it being limited mostly to 10 p.c. of the profits with a minimum allowance payable every year, and on production or sale in Ahmedabad and cotton industry in upcountry centres and to some extent in Bombay also. The majority of the jute mills charge commission on sale proceeds. The system in tea industry is also the same. In the coal industry, the managing agents are usually remunerated either by a fixed percentage on the gross proceeds on all coal sold plus a percentage on other transactions, or by a commission on raisings plus a fixed monthly sum for office expenses or by a fixed percentage on dividends and bonuses paid to shareholders plus a fixed monthly sum for office expenses. In the cotton industry of Sholapur, the remuneration is paid on deliveries. Office allowance is not paid everywhere in the same industry even. Thus in the cotton industry, an office allowance is payable in Bombay but not in Ahmedabad or Sholapur with the exception of one concern in the latter centre. The amount thus paid is not negligible. Thus the maximum amount of commission paid in any year during 1927-37 was in Bombay in 1927 Rs. 25.40 lakhs, in Ahmedabad in 1932 Rs. 39.62 lakhs and in Sholapur in 1927 Rs. 5.65 lakhs, whereas the amount of office allowances has moved between Rs. 4 and Rs. 4½ lakhs during 1933-36, almost equal to the maximum commission paid in Sholapur

during 1927-37. In the sugar industry, in addition to the fixed allowances for office expenses in some cases the managing agents are paid a percentage on the profits and in a few cases a percentage on sales.

We have given so much consideration to this aspect of the question because the commission and office allowances paid to the managing agents constitute an item of cost and therefore exert influence on the determination of competitive position of different firms. It is clear from the above discussion that the mills in Bombay are handicapped because of an office allowance which is not to be found in other centres like Ahmedabad or Sholapur but this disadvantage is more than counterbalanced in view of the fact that commission in Bombay is paid not on the basis of sale or production but on that of profits, a method which has received the approval of many. From the standpoint of business, the latter basis of paying commission is the only one which is fair; for it must on the one hand be in proportion to the services received and on the other it must not impose any unnecessarily heavy burden on the industry. From both these standpoints, the payment of commission on profit basis is justified, for, profit, and not production or sale is the criterion for the judgment of the services received and ability of the industry to pay. A payment on the basis of production gives too much premium on production and is sure ultimately to lead to overproduction; similarly mere sale without profits does not indicate the ability of the industry to pay. In this respect the provision of the 1936-amendment is quite sound; but in so far as it is not applicable to agreements entered into prior to the enforcement of the Act, it remains a deadletter. As regards the office allowance, we have seen that it is not paid everywhere: but in those cases where it is paid it is found unjustifiable in view of the fact that it is paid over and above salaries and other expenses at the offices in the mill premises. *The Bombay Textile Labour Enquiry Committee* rejected it in strong terms. In their words: "If all the actual expenses on salaries, rents and contingencies are met by a company and a reasonable minimum remuneration is paid as commission even when there are no profits or the profits are inadequate, we see no justification for the continuation of the system of office

allowances." When commission is paid on the basis of profits, it so happens that there may be no profits and therefore no commission to the managing agent. Therefore the agreement provides for a minimum sum by way of commission when there are no profits or when profits are inadequate. But if this minimum is high disproportionately to the size and paying capacity of the industrial unit, it becomes a sort of burden and stands in the way of its progress even in good times. So the fixation of the minimum commission should be carefully made.

One thing that has been looked unfavourably by the Indian opinion is that most industries in India, with the exception of those in Bombay and Ahmedabad, are under the managing agency of non-Indians. This not only means the control and management of the industry by non-Indians, but also their exploitation in non-Indian interest and the permanent exclusion of the Indians from them. The matter was brought to the notice of the *Indian Central Banking Enquiry Committee* which pointed out that "since the outbreak of the Great War, there has been a marked increase in the amount of Indian capital invested in Indian industries. . . . Nevertheless, not inconsiderable amount of capital invested in Indian industries is still non-Indian. The result is that the control and management in the case of some of the important industries are even now in the hands of non-Indian firms. The predominance of non-Indian management in some of the important industries has detracted from the value of Indian participation in industrial enterprise. Generally speaking, the managing agents have not given any scope to Indians to hold such positions in the companies they manage as might have a comprehensive idea both in regard to the technique of production and management of the business."

In the old industries, the managing agency system continues. The newly started sugar industry also owes its origin and development to the managing agency system. But conditions are gradually changing and there is already a tendency to start new concerns under the control of a Board of Directors with a wholtime managing director. At this stage it is difficult to appraise the merits or otherwise of the new tendency; but it is sure that unless adequate agencies are developed for

promoting, underwriting and financing, the step cannot be regarded as a wise one. It is true that in Western countries, industries are organised with a Board of Directors at the head; but there they have a class of promoters and underwriters to perform those functions. Until these are developed in this country, the formation of the Board of Directors to the total elimination of the managing agents is neither possible nor desirable. The existing system with disabilities imposed on managing agents, with restriction on their choice of directors, is a better one. But then no hard and fast rule can be laid down; if the new tendency stands the test of time, particularly of the years of depressions, there is nothing to say against it.

Banks as Financiers.

The assistance rendered by banks in matters of the supply of long-term finance to industries is extremely inadequate and it was brought to the notice of the *Indian Central Banking Enquiry Committee* during its investigation. This must however not be taken to mean that no efforts were made in this country to supply long-term finance; but these attempts were either localised or inadequate and based on unsound foundation, pursuing wrong financial policy. During the early days of the *swadeshi* movement, a number of banks supplying long-term finance cropped up, mostly in the Punjab, but most of them could not survive the bank failure in 1913-15. Once more during the post-war boom, a number of industrial banks were registered a list of which is given below, with their paid-up capital and year of registration.

(Source: Basu—*Industrial Finance in India*).

Industrial Bank	Paid-up Capital			Year of Regis- tration.
	Rs.	As.	P.	
1. The Tata Industrial Bank	2,25,19,957	8	0	1917
2. The Calcutta Industrial Bank	79,53,570	0	0	1919
3. The Indian Industrial Bank	3,43,367	5	9	1919

Industrial Bank	Paid-up Capital			Year of Regis- tration.
	Rs.	As.	P.	
4. The Karnani Industrial Bank ...	60,00,000	0	0	1921
5. The Raikat Industrial Bank ...	2,47,000	0	0	1922
6. The Luxmi Industrial Bank ...	1,01,000	0	0	1923
7. The Mysore Industrial Bank ...	6,07,000	0	0	1920
8. The Industrial Bank of Western India ...	39,97,000	0	0	1919

Whatever might have been the original objective with which these banks were started, the fact remains that within a few years of their inception they were found to be carrying on commercial banking business, while the Tata Industrial Bank went into voluntary liquidation in 1923 and was amalgamated with the Central Bank of India. As a result of the wartime prosperity a number of giant commercial banks backed by big business houses have come into existence and will prove a new source of competition to the already existing smaller institutions. Whatever that may be, as yet there is no organised institution on scientific lines to cater for the needs of big industries for long-term finance.

This deficiency in our industrial system is not so much due to the lack of funds in the hands of our banking system as it is due to their conservative outlook and the overcautious policy pursued by the Reserve Bank of India. It may be argued that our banking system has developed on similar lines as that in England; and since the banks carry on business with depositors' money which is deposited for short period, it is financially unsound to lock up these funds in long-period investment. There is much theoretical support behind this argument; but even in England there have been lapses from traditional method under pressure of circumstances after the first great war. In India, however, the banks, including Reserve Bank, have kept strictly aloof from this line of business. Even the recommendations of the *Indian Central Banking*

Enquiry Committee as regards the institution of an all-India Industrial Corporation, when the Central Government and the Legislature are convinced of its need, and the establishment of the Provincial Corporations in the meanwhile have not yet materialised.

In the matter of the supply of current finance, the joint stock banks including the Imperial Bank of India, have played some part, though not a major one. The assistance rendered by banks has taken the form of discounting bills, advancing loans and granting cash credits, overdraft facilities and advances against Government securities and also pledge of stocks. But the method adopted is invariably resented by the Indian industrialists. Even when advances are made against stock, an additional guarantee is demanded by the Imperial Bank and following that, by the joint stock banks. The advances are not made upto the full value of the stocks so pledged, but vary between 60 to 75 p.c. in different parts of the country. The result is that the industries have to meet their long-term financial needs and a considerable part of their short-term needs from other sources. Besides, they do not get the advances against personal credit, but against marketable securities, or stocks, along with the signature of the guarantor; even when advances are made against personal credit, the signature of the guarantor must be there. Cash credit method is however the most popular in this country. Under this system, the advance is made against a promissory note from the borrower, secured by the hypothecation of the stock.

As already hinted, the conservative outlook of the banks causes much hardship and the banking practices are much resented to in this country. While granting credit, the banks do not consider the value of the fixed assets in the hands of the borrowing concern but simply take note of the pledge, which causes an unnecessary hardship to better equipped concerns who under stress of circumstances may have been compelled to come to the banks for assistance. Then, again, they make a discrimination between different classes of goods as regards the value to which advances are made. If the goods happen to be raw materials and semi-manufactured ones, a margin of 25 to 30 p.c. is kept; but in case of manufactured goods it goes as high as 50 p.c. which is too high a figure.

When a concern pledges its manufactured goods and when it happens to be one with reputation, it is sure that it is doing so under stress of circumstances; in that case to advance only upto 50 p.c. is not to solve its difficulty but to put it in an additional one of securing some other source. This however should not be taken as justifying reckless investment; what is being emphasized upon is that when the concern is a reputed one and when it has fallen in temporary difficulty, the banks should not assume a rigid attitude towards it. The method of storing goods also causes much irritation owing to the lack of licensed warehouses. The procedure is as follows. The goods are stored in the godowns of the lending bank, and, when the bank has no godown of its own, in that of the borrower, under letter of hypothecation to the bank. When the goods are stored in the borrower's godown, under L/H, weekly statements have to be submitted to the bank. When the goods are kept in the bank's godown, the borrower, whenever he needs accommodation, must remove goods from his own godown to that of the bank at his own cost; when he needs them back, he must have them removed from the bank's godown to his own, and that too at his cost. This incurring of double expenditure on account of carriage and loading and unloading tells on the efficiency and competitive position of the businessman. When goods are stored in the borrower's godown under L/H, the borrower has to apply every time he needs them back, a process which may have to be repeated several times in a single day if the borrower happens to be a manufacturer and the goods pledged, raw materials. The system of cash credit, though comparatively popular, has its own drawbacks, particularly in times of depression, when elasticity is specially required. In the words of the *Tariff Board Report on the Cotton Textile Industry (1927)*, "The evidence before us tended to show the system of cash credit has drawbacks in times of depression when elasticity is specially required, not only because the amount is repayable at short notice, but also because, when prices are falling, the banks have to call on the mills to reduce their cash credits or to increase their securities, as the securities, on which they have advanced, have deteriorated in value, and this happens at a time when it is obviously specially difficult for the mills

to adopt either of these courses." Finally the attitude of the banks as regards repayment is also extremely rigid. In business matters too much emphasis on "due date" of repayment causes unnecessary hardship; nor is there any reason for putting too much emphasis on it when advances are secured by goods and guarantee. If repayment is not made on due date; the borrower will be paying interest on it; notwithstanding all these considerations, the Indian banks are too strict. Possibly they smell danger in everything; but danger cannot be averted by this type of over-cautiousness which, on the contrary, hampers business. The banker must consider beforehand to what extent he is ready to go and in what lines; but once the decision is taken, the assistance rendered must not be half-hearted, but full. In the words of Manu Subedar, "A closer examination of values and margins, no bank can afford to neglect at any time, whether it is boom or depression, but an undue emphasis on due dates and repayments with regard to loans to industrial concerns can intensify a downward situation, against which industry may be fighting."

Public Deposits as a Source of Finance.

Bank credit is not popular in certain quarters, as in Ahmedabad, for two reasons—first, the hypothecation of goods with the bank is considered as a sign of weakness and therefore the credit of the concern deteriorates in public estimation, and second, the hypothecation of goods involves some visible control of the industry by the bank, which is resented to. As a result of this, a system of public deposit has been developed to a very great extent in Ahmedabad and to some extent in Bombay. In its origin, the system of keeping deposits with industrial concerns was "undoubtedly a reflex and a transformation of the old system of money kept for safe custody with the *mahajan*. Its survival even in these days would lead one to believe that the system must have worked fairly satisfactorily for both sides for long past." It was found at the time of the investigation of the *Central Banking Enquiry Committee* that the Ahmedabad public considered it safer to deposit with a mill than with a bank and this state of affairs was attributed to the business integrity of the people in

charge of the management of the mills who looked to the interests of the depositors. Since the first great war, the deposits in Ahmedabad from rural areas had declined, "due partly to decline in the prosperity and partly to the competition of the Government," and the gap was filled up by the accumulated reserves of some of the industrial concerns which had flourished and which were inter-deposited. "On the whole there has been no reduction or falling in the total of the deposits received by mills which have continued steadily during a long period of twenty-five years." In Bombay, however, the system of deposits has declined "owing to the counter-attraction of the interest obtainable from postal cash certificates and government loans, the banks' policy of obtaining a charge on the stocks of the borrowing concerns and thereby reducing the security available to the depositors and the inconvenience and loss sustained by a proportion of the depositors owing to the inability of a small number of mills to repay the deposits on the due dates or at all." In other parts of India the system of deposits is unknown except in Bengal where in one or two cases deposits have been obtained "from the officers of the company as well as from the public," though in the latter place the system is not widely known nor firmly established.

It is the characteristic feature of these deposits that they are not secured by anything. The members of the public who offer them rely only on the reputation and financial condition of the concern and also on the standing of the managing agent under whom it is working. The deposits are generally for a short period of six months to one year and are usually renewed thereafter. In Ahmedabad, deposits for a longer period of even seven years are to be found. There is no fixity as regards the rate of interest but it varies according to the standing of the concern, and that of the managing agents. Some industries used to obtain deposits at a lower rate than the banks.

From theoretical standpoint, the system "presents great dangers, since it is contrary to the principle of sound finance to use loans repayable at short notice for the purpose of fixed capital." When the industry faces bad days, the deposits, which are so essential at that time, are likely to be withdrawn,

even though the bad days may be short-lived, thereby prolonging the difficulties of the industry. Side by side with the factor comes another factor, inelasticity. The proverbial carrying of coal to New Castle may be the case with certain concerns and while others may be suffering from a dearth of it. Thus while excess of deposits will be a financial burden on the former, a lack of it would be the cause of inefficiency for the latter. Even when the less reputed concerns attract deposits, they have to pay a higher rate of interest in competition, and thus while the problem of financial inadequacy is solved, another problem crops up in the shape of higher cost. It is peculiar that even with the same concern, the rate of interest varies according as its standing in public estimation goes up or down. No more secure is the position of the depositors. In the first place, the deposits are insecure loans, without any condition being imposed as regards the precise nature of their use. This being so, the funds thus obtained have at times been used for speculative purposes with consequent loss. This is one of the reasons why the popularity of the system declined in Bombay, though the same cannot be said of Ahmedabad. The loans being unsecured, the depositors cannot have a say in the matter of industrial management and the directors have their fullest discretion. And secondly, the selection of the avenues of investments is a difficult task for the majority of the depositors. It is very difficult even for organised expert institutions, not to speak of lay depositors, to judge from outside the financial standing of a concern, so much window-dressing covers the actual position.

But whatever may be said from theoretical stand-point the merits or otherwise of the system are to be judged from the results achieved, and from this stand-point the system has so far justified itself in Ahmedabad. The position of the depositors, no doubt, appears insecure at first sight; but in India where, at least in business, words once uttered are more important than the letters of law, the position of the depositors is not so insecure as is often made. For the managing agency firms are so much anxious to maintain their credit that they would prefer financial loss to loss of credit. Yet in these days it is desirable that wherever complexity is expected,

things should proceed through scientific channel. But there I cannot see eye to eye with the suggestion of Panandikar that "the intervention of a bank between him (the depositor) and the concern would make his deposit much safer, because the bank with its organisation would know the concerns to whom to lend money and the time and period of lending it and would be able to exercise some control over their assets." For, anyone who is familiar with the banking policy and practice, of which something has already been said, would not suggest this course, which would mean an evaporation of even this source wherever available. A more scientific course would be the organisation of investment trust, through which all investments, both short and long period, would be made. This would organise the depositors on the one hand and organise the investment on the other. In another chapter we shall give some consideration to the problem of organising investment trusts in this country.

Share Capital

The financial basis of the structure of the mill industry is share capital, the only exception being Ahmedabad where share capital occupies the second position yielding the first one to public deposits. The proportion of share capital to the total working capital plus fixed assets is not of course the same but varies from one centre to another and from one unit to another. According to the Special Tariff Board on Cotton Textiles, the ordinary and preference paid up capital of the Bombay mills represent little more than one third of their original fixed capital expenditure on block, and the paid-up capital of the Ahmedabad mills represents barely one-fourth of their original block value. According to the *Bombay Textile Labour Enquiry Committee*, "these proportions to the gross block account for Bombay, Ahmedabad and Sholapur are 38, 25 and 13 per cent. respectively." In the jute industry we have already seen that the practice is for the managing agent to pass over the shares to the members of the public, keeping only a negligible proportion in their hands. In the coal industry, according to the Indian Coal statistics of 1935, 66 coal companies had an aggregate

paid-up capital of Rs. 623 lakhs. In the sugar industry we have already seen that the tendency in recent years has been to start concerns with board of directors to the total elimination of managing agents and raising capital by the issue of shares. In Cawnpore also, share capital constitutes a major portion of the industrial finance. The proportion of paid-up capital to gross block account can be seen in the following table, wherein figures are given for 8 mills, except in 1936, wherein these are for 11 mills.

Source: Cawnpore Labour Enquiry Committee Report.

Year	Paid-up Capital	Total Block Account*
	Rs.	Rs.
1929	32526215	46073998
1930	22540515	47166914
1931	22525380	47741530
1932	22525380	48603891
1933	22525430	49600488
1934	22554620	51242309
1935	21179620	53979181
1936	22754620	59786860

The Share Capital of a Company can be classified variously—from the standpoint of capital structure, of dividend, and other rights, and of the method of transferring them. From the standpoint of capital structure, three types of capital may be distinguished—Authorised, Subscribed and Paid-up. The authorised capital is the total nominal value of shares which a company is authorised by its memorandum to issue. Subscribed or issued capital is the nominal value of shares actually issued. Paid-up capital is the amount actually received, or credited as received, from the members. A few more types follow from the above. Thus the whole of the issued or subscribed capital is not called up, but only a part of it. That part which is actually called up is called-up capital, the rest, uncalled capital.

* Total block account does not include amount written off under Capital Reduction Schemes, while Paid-up Capital figures are shown after such reduction.

Out of the called-up capital, a part may be paid-up immediately, the rest being due, to be paid within a stated period. Reserve capital is that part of the uncalled capital which by special resolution has been declared incapable of being called-up except in case of winding. One weakness from which the capital structure of many concerns suffers is that the gap between authorised and subscribed capital, and subscribed and paid-up capital is unusually wide. It is of course true that authorised capital must be high in order that in future the concern need not suffer from lack of capital owing to legal handicap. It is well known that the Memorandum of Association contains a capital clause, which, like any other clause, is unalterable without special procedure which may mean botheration and wastage of time. That is why, high authorised capital is taken at the inception. But this has two drawbacks. In the first place, the investing public, most of whom have no great knowledge about capital structure and who do not get any expert assistance in these matters owing to lack of it, are duped by high authorised capital. And secondly, a lack of legal restriction may lead to the growth of mushroom concerns with high authorised capital but little paid-up capital, leading ultimately to their collapse. So far as the banking companies are concerned, the recent amendment of the *Indian Companies Act* (Act IV of 1944) has made some good provisions, viz., that no banking company incorporated under this Act on or after 15th January, 1937 shall commence business unless shares have been allotted to an amount sufficient to yield a sum of at least Rs. 50,000 as working capital and that no banking company incorporated on or after 15th January, 1937, whether within or without British India, shall, after the expiry of two years from the commencement of the Amendment Act of 1944, carry on business in British India unless it satisfies the following conditions: viz. that the subscribed capital of the company is not less than half the authorised capital and the paid-up capital is not less than half the subscribed capital. Some legal restriction of this character will be of help in case of other companies as well.

Another classification arises from the standpoint of dividend and other rights. From this standpoint, the shares

may be classified as ordinary, preference, deferred and miscellaneous. Obviously this classification is necessitated in order to give different attractions for investment to different classes of persons according to their psychological make-up. In general, there are three classes of persons in the investment world, whom Nixon has given the names of Mr. Cautious, Mr. Speculative and Mr. Medium. Mr. Cautious is extremely cautious in matters of his rights, no matter however poor reward his investment may fetch; Mr. Speculative is just the reverse and would go to any extent, irrespective of any security, if he smells gain, no matter if his expectations be false. Mr. Medium follows the golden middle path, investing in ordinary shares. A generation or so ago, even in England, the share capital of nearly all companies had only two classifications—ordinary and preference. To-day however, there are as many classes of shares as the ingenuity of the directors and Promoters can devise, but the two principal types are ordinary and preference. As a result of the over multiplication of types, to-day the name of a particular share is no sufficient guide to the exact nature of the rights to be enjoyed. These rights are however defined by the prospectus or other documents on which the shares are offered and by the Articles of Association of the Company. For an ordinary share in itself means nothing but has to be defined to be understood. Sometimes different names are used in different countries for the same class of shares. There the difference is only one of nomenclature. Thus the share capital of a company is frequently described in U. S. A. and Canada as the Capital Stock, and the word 'Preferred' is used to denote the same thing as preference. In England and India, a distinction is made between stocks and shares, and the companies describe their capital usually as either stocks or shares, but not both. In these countries, stock is used to denote a form of capital which has no division into shares and no distinctive numbers. Any portion of a company's stock is described simply by its nominal value. The stock is however an uncommon form of industrial paper in India, possibly due to low incentive to invest in this country. In the same way, unlike the American and Canadian practice, we make a distinction between preference and preferred shares, the preferred shares usually ranking after preference.

A study of the stock capital is one of theoretical interest in this country, in view of the fact that it is not common in this country. The origin of the word and how it came to indicate the capital structure of the industry has been very humorously described by Hartley Withers. He points out that "the word 'stock' has meant many things in the course of its versatile career. From a trunk of a tree, it was by a natural metaphor applied to the original line of a family..... it gradually came to mean something heaped up like a stack or stook and to some sort of accumulated store. In this sense it still survives in the phrases, 'stock-in-trade,' meaning the goods on hand held by a manufacturing or trading company and 'Taking Stock,' meaning the process of counting and valuing the stock-in-trade. A passage in Bacon, however, shows that he used it as a store of bullion. 'Let the exportation of home commodities,' he says in his Advice to Villiers, 'be more in value than the importation of foreign, and the stock of the kingdom shall yearly increase; for then the balance of trade must be returned in money or bullion.' Doubtless it was in this sense of a store of money that Ben Jonson used it—'prodigal men feel not their own stock wasting.' From this sense the transition was easy to the meaning in which the word is generally used by Adam Smith, *viz.*, the capital of a firm or company, that is to say, the monetary resources which have been invested in its business or kept in hand for its daily needs. Proceeding in its evolution, the word transferred its meaning to the securities received by those who subscribed the capital of companies, and then divided itself again to mean marketable securities in general, and a certain kind of marketable security in particular."

As already noted, stock has no division into shares and no distinctive numbers, with the consequence that the stock may be transferred in fractional parts. In order to be the holder of shares, one must hold a share or a number of shares which is to be in its unit, say for Rs. 500; but he may be the holder of stock for any fractional parts of that unit, say, Rs. 200. In another respect, stock differs from shares, *viz.*, that stock is always registered or inscribed, while shares may or may not be such, and be only bearer securities. The following are the different types in use:—

1. **Debenture Stock**—When there are no series of equal amount and no fixed numbers, and only one debenture certificate is issued for the full amount taken by each debenture stock-holder, known as debenture stocks. They have a priority of security on the whole undertaking of the company and ranks first over other classes of stock in respect of payment of interest and principal.

2. **Guaranteed stocks** are next in order of security to the debenture stocks, but enjoy a prior right over other types as to the return of capital, and payment of dividend. Guaranteed stocks are usually cumulative in character.

3. **Preferred stocks** enjoy a prior claim to a fixed dividend but, unlike preference shares, are not cumulative in character.

4. **The ordinary or common stocks** enjoy no guarantee or preference. The outcome is therefore subject to the uncertainty and fluctuation of the result in the working of the company. The ordinary stock is at times divided into preferred ordinary and deferred ordinary,—the former being entitled to a certain rate of dividend each year if profits are earned, and the latter to whatever rate out of the remaining profits.

Turning next to the share capital of the company as formed in India, we find, broadly, three different types—ordinary, preference and deferred. We shall take them up one by one. Although the different types of share capital available in Indian industry bear the same name as in other countries, yet there are certain distinguishing features both in the proportion of security offered to different classes of shares and also in the manner in which they are secured. To take up first the ordinary shares, they are those shares which are not entitled to any preferential treatment either as regards the payment of dividend or repayment of capital in case of winding up, but enjoy any profits that may remain after the claims of different funds a company may have have been satisfied and interest on borrowed money and dividend on preference shares, along with any part due to cumulative preference for previous years have been paid. In case no profit is earned, the ordinary share-holder goes without any-

thing. But as one writer has rightly said, the ordinary shares are not so ordinary as the name suggests; on the contrary, they are the life-lines of the industry. Preference shares impose a burden, so to speak, on the industry and are not liked, unless ordinary shares are not in a position to offer sufficient attraction to the investing public.

In some cases, the ordinary shares are divided into two or three types, the difference between them being slight. Thus the Comilla Union Bank Ltd., has two types of ordinary shares—'A' shares of Rs. 50 each and 'B' shares of Rs. 25 each. In Singaran Coal Syndicate Ltd. ordinary shares are divided into two—ordinary and B ordinary, both of Rs. 2-8-0. each. The B shares have a preferential claim to a dividend of 7 per cent. and after the ordinary shares have received a similar distribution, the shares rank *pari passu* in all respects. In the Grob Tea Co., Ltd. both A ordinary shares of Rs. 10 each and B ordinary shares of Rs. 5 each rank *pari passu*. In the Murphulani (Assam) Tea Co., Ltd., there are ordinary and preferred ordinary shares. The preferred ordinary shares carry the right to a fixed non-cumulative preferential dividend at the rate of 5 per cent. per annum and to participate in the surplus profits available for dividend rateably with ordinary shares in proportion to the respective capital paid-up thereon. The preferred ordinary shares also carry preferential claim to repayment of capital and to participate rateably with the ordinary shares in the residue, if any, of such surplus assets as shall remain after paying off the ordinary capital of the company. Sometimes it so happens that a company has originally only one type of ordinary shares but afterwards takes another type. Thus the Basti Sugar Mills Co., Ltd. increased its capital in 1943 by the creation of B shares, the original shares being classified as A shares. B shares rank *pari passu* with A shares in all respects except that they do not carry voting rights. The Bengal Bonded Warehouse Association has four types of ordinary shares—A shares of Rs. 500 each, B shares of Rs. 62-8-0 each, C shares of Rs. 100 each and D shares of Rs. 12-8-0 each—all shares carrying equal rights. The Bombay Burmah Trading Corporation Ltd. has three types of shares—100 shares of Rs. 2,500 each, 40,000 old shares of Rs. 125 each and 84,000

new shares of Rs. 125 each. The first variety is entitled to receive an extra or preferential dividend equal to one-third of the surplus profits remaining in any year after paying a dividend of 12 per cent. per annum on all shares in the company, including these 100 shares, and after setting aside any sums to the credit of Reserve Funds as the directors may decide. In the Digwarrah Rubber Co., Ltd. there are ordinary and preferred ordinary shares, the latter being issuable as fully paid in conversion of debenture bonds at debenture-holders' option, with non-cumulative preferential dividend of 7 per cent. per annum ranking *pari passu* with ordinary shares for further distribution. In the Indian Tarpendine and Rosin Co., Ltd. there are ordinary Government A shares and ordinary B shares, both of Rs. 10 each. In the Titaghur Paper Mills Co., Ltd., there are A ordinary shares and B ordinary shares of Rs. 5 each, ranking *pari passu* with each other in all respects except in voting power. The above is an expansive list of the different types of ordinary shares available in this country and it shows clearly the rights attached to each type.

The popularity of shares depends not only on the rights attached but also on the denomination of shares, the more so in this country where many investors are people with small resources. The general tendency is for the shares to be of higher denomination in Bombay than in Calcutta. In the cotton industry the shares ranged from Rs. 500 to Rs. 1,000. Only in recent years has there been a tendency for the shares to be split up into smaller denomination. In Bengal the shares are sold in lots of 100 in case of Rs. 10 shares and of 25 in case of shares of higher denomination. But the smaller denomination in itself means nothing unless the minimum number of shares which can be purchased by a single investor is reduced.

We shall turn next to preference shares. The purpose of offering preference shares is to attract as large a capital as possible from the members of the investing public. Although the preference shareholder is as good or as bad a proprietor of the concern as the ordinary shareholder, the preference share is a burden on the concern and therefore its proportion to the total share capital should be carefully

determined. For too much dependence on preference shares would mean a burden on the concern on the one hand, and a deprivation of the ordinary shareholders on the other. No less important is the dividend allowed on preference shares. If this dividend is high, as it is in India, the ordinary shareholders have to go without any dividend in lean years in particular, and get low rate in general. In India, possibly, with a view to give greater attraction to the investors' fund, a large number of concerns have got preference shares in their portfolio, most of them being cumulative preference shares. Only in case of insurance companies, preference shares are to be found in case of one or two concerns. The largest number of companies having preference shares are to be found in the jute industry. An idea as to the number of companies having different classes of preference shares can be had from the following table:

Compiled from *Investors' India Year Book*, 1942-43.

TABLE.

Type of Preference Shares,	Coal Industry.	Cotton Industry.	Jute Industry.	Tea Industry.	Sugar Industry.	Engineering Industry.	Miscellaneous Industries.
Cumulative	6	28	49	20	9	10	34
Non-cumulative	—	1	—	1	—	—	—
Participating	1	—	3	2	3	—	2
Redeemable	1	4	1	1	5	—	1

The above gives a rough idea as to the place occupied by different types of preference shares in different industries. No figures are available as regards the proportion of preference shares in the capital structure of a concern; but a rough estimate shows that in jute industry it is slightly more than 40 p.c. and in cotton industry even less than 20 p.c. The maximum proportion is to be found in the Tata Iron & Steel Co. where it constitutes about 70 p.c. of the total capital. This excessive dependence on preference shares is theoretically unsound and practically obnoxious as is evidenced by

the history of the Tata Iron & Steel Co during the twenties. (cf. Lokanathan, *Industrial Organisation in India*.)

The preference shareholders enjoy preferential rights in several directions. In the first place, they enjoy a preferential claim to dividend which in most cases is cumulative in character, i.e., if the profits of any year are insufficient to pay full dividend on such shares, then no dividend can be paid thereafter on ordinary shares until all arrears of preference dividend have been paid in addition to that for the current year. If the claim to dividend is non-cumulative, then the preference shareholders will only be entitled to it provided profits are earned. Sometimes preference shareholders are made to be entitled to share the surplus profits, if any, with ordinary shareholders in addition to the fixed rate of dividend upon defined terms; then the shares are known as participating preference shares. Another type of preference shares which is new so far as this country is concerned, and which has been introduced by the Indian Companies Amendment Act of 1936, is known as Redeemable Preference Shares. Under this Act a company, if authorised by its articles, may issue preference shares redeemable out of profits, or out of the proceeds of a fresh issue of shares or out of the sale proceeds of any property of the company. The preference shares may be tax free or taxable. Secondly the preference shareholders enjoy a preferential right to the assets of the company in case of liquidation. Let us illustrate the above types of preference shares from Indian cases.

In the field of banking only a few banks have taken preference shares. Thus the Allahabad Bank, Ltd., has got 6 p.c. tax free cumulative preference shares of Rs. 100 each carrying preferential claim to repayment of capital. The Habib Bank, Ltd. has 3 p.c. taxable cumulative preference shares of Rs. 100 each carrying preferential claim to repayment of capital and also the right to participate in the profits at the rate of $\frac{1}{4}$ p.c. for every 1 p.c. dividend paid to ordinary shareholders over 6 p.c.; they also carry the further right to participate in any bonus declared to be paid at the same rate as payable to ordinary shareholders. In the Hooghly Bank, Ltd., 6 p.c. tax free cumulative preference shares carry the right, in case of winding up, to repayment of capital and arrears of dividend

whether declared or not up to the commencement of winding up, in priority to ordinary shares and may be paid off at any time on 6 months' notice, after 1st January, 1960; or be converted from that date, at the option of holders, into ordinary shares in the proportion of 10 ordinary shares for one such share. Sometimes a concern has preference shares combining both cumulative and non-cumulative dividend. Thus the Khas Kajora Coal Company, Ltd., has preference shares carrying the right to a fixed cumulative preferential dividend of 5 p.c. per annum and to a non-cumulative dividend of 3 p.c. per annum and also the right to participate in a further dividend of 2 per cent. per annum rateably with the ordinary shares after the latter have received a dividend of 8 p.c. per annum, all further profits remaining going to ordinary shares. They also enjoy the preferential claim to repayment of capital and arrears of dividend. The Bengal Jute Mill Co., Ltd., has $5\frac{1}{2}$ p.c. tax-free redeemable cumulative preference shares, redeemable at the option of the company in whole or in part out of the profits of the company at any time or times at a premium of Rs. 12 per share. In the Birla Jute Manufacturing Company, Ltd., the cumulative preference shares carry preferential rights to repayment of capital, and also the right to participate in any year in any divisible profits (at the discretion of directors), after the ordinary shares have received dividend of 50 p.c. Here the dividend on ordinary shares is fixed at too high a figure and when this is given, the preference shareholders can claim participation. At times the maximum extent to which the preference shareholders may participate in the profits is limited. Thus in the Craig Jute Mills, Ltd., the participating preference shares carry the right to a fixed cumulative preferential dividend of 5 p. c. per annum, and after the ordinary shares have been provided with a similar dividend, these shares shall have the right to participate in a further dividend of 1 p.c. per annum rateably with ordinary shares upto a maximum of 10 p.c. In the same way the maximum extent of participation in the case of the Waverley Jute Mills Co., Ltd., is also 10 p.c. In the case of the New Indian Sugar Mills, Ltd., the maximum extent of participation is 9 p.c. This company has two types of preference shares—participating and convertible redeemable

—the convertible redeemable preference shares carrying the right to a fixed cumulative tax-free preferential dividend of $7\frac{1}{2}$ p.c. per annum; such dividend shall rank before ordinary shares but after the participating preference shares. These shares, in a winding up, rank *pari passu* with ordinary shares, and at the option of the holders, they may at any time be converted into ordinary shares at par. The Gwalior Sugar Company, Ltd., has two classes of shares—preference and redeemable preference, the company having discretion to redeem the whole or any part of the latter. So long as these shares remain unredeemed, the rights attaching to these shares and preference shares are the same as if they belong to one and the same class.

Some of the companies belonging to the miscellaneous group make an interesting study as regards the preference shares. Thus the Imperial Chemical Industries (India), Ltd., guaranteed to provide sufficient funds each half year to enable the Alkali and Chemical Corporation of India Ltd. to pay preference dividend in full for a period of 5 years from 1st April, 1938. The participation in case of preference shares in the Dalmia Cement, Ltd. is, so to say, progressive in character, increasing with an increase in the dividend declared on ordinary shares. Thus it will be 7 p.c. in the event of a dividend of 10 p.c. being declared on ordinary shares, to $7\frac{1}{2}$ p.c. in case of a dividend of 20 p.c. and above being paid on ordinary shares and also to an additional $\frac{1}{2}$ p.c. rising upto 9 p.c. per annum along with every 10 p.c. further rise in the dividend on ordinary shares without any further right to participate in profits or assets. In the Sree Gopal Paper Mills, Ltd., the 6 p.c. preference shares also carry the right to participate in the profits available for dividend to the extent of 25 p.c. of the surplus of such profits remaining after payment of a dividend of 10 p.c. on ordinary shares, but the dividend payable on these shares in respect of any one year shall not exceed 8 p.c.

The ultimate control of a concern generally rests with ordinary shareholders, the preference shareholders, in general, having nothing to do with it. Only in extreme cases are they given any such right, being unknown in this country, so far as I know. Sometimes, the preference shareholders are given

the option of converting their preference shares into ordinary ones when the latter provide sufficient attraction for the same. Of this one or two cases we have already noted. This type of shares is issued in order to give sufficient attraction to "speculative investors who like to take a chance, provided it is not too great." Another variety of preference shares has come into use in countries like England and U. S. A. and is not entirely unknown in this country as well. In this, there is a variety of preference. Thus the American Corporations sometimes use two or more types of preferred stocks, such as first preferred and second preferred or Preferred A and Preferred B. Generally, the first mentioned preferred stock enjoys certain preference in dividend payment over the second variety, while both these types enjoy preference over the common stock. In England preferences are not of one or two types, but at times exceed a dozen in number. In recent years, owing to legal handicaps, the practice is coming in vogue in America not to name the stock as preference in order to distinguish it from common, but classify them as Common A, Common B, etc., in order of preference granted. In India also some concerns follow the above practice. In Ahmedabad Manufacturing and Calico Printing Co., Ltd., there are A $4\frac{1}{2}$ p.c. tax-free cumulative preference shares of Rs. 125 each, $4\frac{1}{2}$ p.c. taxable Diamond Jubilee second preference shares of Rs. 50 each and $4\frac{1}{2}$ p.c. taxable cumulative 3 p.c. preference shares of Rs. 50 each. In Ajit Mills, Ltd., there are $5\frac{1}{2}$ p.c. tax-free cumulative A preference shares of Rs. 100 each, $4\frac{1}{2}$ p.c. tax-free cumulative B preference shares of Rs. 100 each, and 5 p.c. tax-free cumulative C preference shares of Rs. 100 each. As between themselves, they rank equal in all other respects. In the Bowreah Cotton Mills Co., Ltd., there are 8 p.c. tax-free A cumulative preference shares and 7 p.c. tax-free B non-cumulative preference shares. A preference shares carry preferential claim to dividend and repayment of capital prior to B preference and ordinary shares, and B preference shares carry preferential claim to dividend only, prior to ordinary shares, but as regards capital, these shares rank *pari passu* with the ordinary. In the jute industry, the Clive Mills Co., Ltd. has 6 p.c. tax-free cumulative preference shares and 7 p.c. tax-free cumulative A

preference shares. The A preference shares rank after 6 p.c. preference shares both for dividend and repayment of capital.

But, for that, too much importance should not be attached to the preferential aspect of these shares, for "in practice, every preference accorded to preferred stock is usually balanced by a limitation, most preferred stock is neither fish, nor fowl, nor good red berry." For when the concern is not running successfully, it possesses the income weakness of debentures and risk of shares, while at the same time not enjoying safety of the former and fat earnings in prosperous years of the latter. In times of difficulty, it may be thought that the preference shareholder is much better off than the ordinary one; nothing of the kind. It is not that whenever a difficulty arises, the concern will be liquidated; in extreme difficulty, some sort of reorganisation may be effected but even then ordinary shareholders possess greater advantage in view of the fact that "the organised control of the common stock, represented in the board of directors, usually gives this class of stock a relative advantage over the unorganised preferred stock in such a process." At times, the preference shareholders may have to forego certain advantages. Thus in the New Victoria Mills Co. Ltd., under a scheme of reorganisation in 1930, reduced 550,000, 8 p.c. cumulative preference shares of Rs. 10 each to 321,100 6 p.c. cumulative preference shares of Rs. 5 each, the remaining shares being cancelled. In case of the Craig Jute Mills Co., Ltd., the rate of dividend on preference shares was reduced from Rs. 100 to Rs. 50 and the rate of dividend thereupon from 9 p.c. to 5 p.c. per annum and all rights to cumulative dividends unpaid from August, 1929 to January, 1940 were cancelled. So also in case of the Waverley Jute Mills Co., Ltd., the rate of dividend on preference shares was reduced from 8 p.c. to 5 p.c. per annum and all rights to cumulative dividends unpaid from August, 1929 to January, 1940 were cancelled. In the Nambarnadi Tea Co., Ltd., all arrears of the cumulative preferential dividend were cancelled and the holders of such shares were given in lieu thereof one Income Certificate of Rs. 100 for every 20 preference shares held by them, carrying interest at 5 p.c. per annum. The existing preference shares of Rs. 10 each were converted

into ordinary shares of Rs. 10 each, fully paid up, ranking for dividend and in all other respects *pari passu* with the existing ordinary shares of the company. It may be asked, why the preference shareholders agree to have their rights curtailed? The answer is obvious. If they do not, they will be greater losers. For what is needed in times of difficulty is to reduce financial burden. One such process is a reconstruction of capital structure, in which the major burden falls on preference shareholders. If they do not agree to a reconstruction scheme in which they have to undergo some sacrifice, they may have to incur greater loss owing to the total collapse of the company. Thus it is clear that although preference shareholders enjoy certain preferences and ordinary shareholders do not, yet the ordinary shareholders are not altogether ordinary and preference shareholders may have to undergo considerable sacrifice. Yet the very name is attractive and gives attraction to a class of investors.

But even then the investor must take note of a point or two before taking decision to subscribe to the preference shares. For otherwise his psychological make-up may receive the greatest set-back owing to non-fulfilment of expectation. Thus the investor must make sure that the company is one which enjoys an income which is much above the amount payable as preference dividend. For, if this amount of income is high, the preference shares will also be in a stronger position and be more attractive. In a marginal case, the investor is always at suspense as to when he may be called upon to sacrifice a part of his rights. No less important is the stability of income of the company; for if it is not stable, the preference shares will depreciate in value whenever the income goes down. The capital structure of a concern is another important factor worth consideration. If it is overburdened with financial obligations, its preference shares cannot be attractive, however great the concern may be, unless of course the stability of income and a big margin in income over preference dividend counterbalance this factor.

Sufficient has been said about preference shares. Next we turn to another type of shares, *viz.*, deferred shares, alternatively known as Founders' shares. The name itself is significant as regards their proper character. It is well-known that the

Founders of a concern exercise a good deal of their brain and spend a lot for making preliminary arrangements for promoting a concern. They form a privileged class of shareholders, a fact which justifies its name as founders' share. They are deferred in so far as they come in to have a share after a certain per cent. dividend is declared on ordinary shares. But a characteristic of this type of shares is that the deferred capital constitutes a small portion of the total capital structure and they are small in denomination in general.

In India, too much importance cannot be attached to this class of shares since they are to be found in only a few cases. This is probably due to the existence of managing agents who continue to serve even after the promotion work is over, and who have other sources of income. Only in a few instances therefore deferred shares are to be found in use, of which a few we shall note here. Thus the Bank of Behar Limited has deferred shares of Rs. 25 each which, after being fully paid up, are entitled to receive a fixed tax-free dividend of 3 p.c. per annum payable only after a minimum tax free dividend of 7 p. c. and 5 p.c. per annum is paid on ordinary and preference shares respectively. In a winding up these shares shall not be entitled to any surplus assets and in case of deficit shall be liable first to make it up. In the cotton industry there are a few instances in which the company has taken deferred shares. Thus the E. D. Sassoon United Mills, Ltd., has, out of the authorised, issued and subscribed capital of Rs. 250 lakhs, raised Rs. 50 lakhs by deferred shares of Re. 1 each. Here the ordinary shares are entitled to a preferential dividend of 6½ p.c. and after the deferred shares have received a similar dividend, the residue is to be divided equally between ordinary and deferred shares. In the New Victoria Mills Co., Ltd., the deferred shares are entitled to participate in dividends upto 10 p.c. per annum after the preference shares have received a cumulative dividend of 6 p.c. and ordinary shares have received 10 p.c. Any surplus divisible profit remaining thereafter are to be apportioned in three equal parts for payment of further dividend to the preference, ordinary and deferred shares. In the R. G. Cotton Mills Co., Ltd., after the payment of 6 p.c. cumulative preference dividend along with 2 p.c. non-cumulative preference

dividend per annum, the deferred shares rank *pari passu* with ordinary shares up to a dividend of 10 p.c. per annum, and when any surplus profits are available for distribution in any year, the deferred shares are to receive one-half and the other half is to be paid to ordinary shares. In case of winding up, the preference, ordinary and deferred shares rank *pari passu* in all respects. In the jute and sugar industries, the solitary instances of concerns having deferred shares are India Jute Co., Ltd., and South Behar Sugar Mills, Ltd., respectively. In the case of the former, the deferred shares receive the same percentage of dividend as ordinary shares upto 6 p.c. only. In the South Behar Sugar Mills, Ltd., the deferred shares are entitled to a dividend upto 10 p.c. after 10 p.c. dividend has been paid on ordinary shares; any surplus remaining will be divided equally between ordinary and deferred shares. The iron and steel industry is however the only one in which most of the few concerns that we have have got deferred shares. Thus the Indian Malleable Casting Ltd. has 154,000 deferred shares of Re 1 each. After the ordinary shares have received a fixed taxfree dividend of 3 p.c. per annum, any surplus remaining will be distributed equally between ordinary and deferred shares. In a winding up, the ordinary shares rank in priority to deferred shares; any surplus assets remaining after the whole of the paid up capital is paid off, will be distributed between the ordinary and deferred shareholders each receiving one-half of them. The deferred shares of the Indian Steel and Wire Products Ltd. are entitled to half the surplus profits remaining after payment of a 6 p.c. dividend per annum on ordinary shares and to half the surplus assets, in case of winding up, after the paid-up capital is fully repaid. In the Mukand Iron & Steel Works Ltd., after the ordinary shares have received a non-cumulative dividend of 8 p.c., the deferred shares will get a non-cumulative dividend of 25 p.c. and any surplus profits available will be distributed equally between the holders of ordinary and deferred shares. In case of winding up, the preference capital will be paid off first and after that the ordinary and deferred capital rateably. If any surplus remains after all these payments have been made it will be distributed between the holders of ordinary and preferred shares in the proportion of $\frac{2}{5}$ ths and $\frac{3}{5}$ ths respect-

ively. But the most noted of the deferred shares in this country in general and in iron and steel industry in particular, not only because of the richness of the issuing concern but also because of the highly speculative character, are those of the Tata Iron & Steel Co., Ltd. These shares are entitled to a non-cumulative dividend of 25 p.c. per annum after the dividends have been paid on preference shares and 8 p.c. non-cumulative on ordinary shares. Surplus profits, if any, are payable, half to the ordinary and half to the deferred shareholders. Among other concerns having deferred shares, mention may be made of the Aluminium Corporation of India, Ltd., Assam Bengal Cement Companies Ltd., Balmer Lawrie & Co., Ltd., Dalmia Cement Ltd., etc. No special feature characterises them and therefore needs no mention.

We have already remarked that the object of offering as many types of shares as the ingenuity of the directors can devise is simply to offer as much attraction to investors as possible and to attract capital from all possible sources. We have studied three distinct types of shares as are to be found in this country. Apart from these, there are various other types, which may conveniently be classified as miscellaneous, and the exact nature of which may briefly be noted. The Mymensingh-Bhairabbazar Railway Co., Ltd., has guarantee shares and rebate shares, the former carrying a guarantee from the Government of India of $3\frac{1}{2}$ p.c. per annum and are a trustee investment. The nett earnings of the company are divided between Guarantee and Rebate shares in the proportion of $63/86$ and $23/86$ respectively. When the Rebate shares' proportion of the nett earnings is less than 5 p.c. on the Rebate capital, the balance is paid as rebate by B. & A. Ry. upto a maximum of $23/86$ of the nett receipts derived from traffic interchanged by this Railway with the Mymensingh-Bhairabbazar Railway Co., Ltd. If and when the nett receipts of the company for any year shall exceed the sum required to pay the management expenses and interest at 5 p.c. per annum on the share capital of the company, the excess shall be divided equally between the company and the working agency. In the Elgin Mills Co., Ltd., there are vendors' shares ranking *pari passu* with ordinary shares. The Madhewji Dharamsi Manufacturing Co., Ltd. has got conversion shares along with deferred shares. The Namburnadi Tea

Co., Ltd., has got 5 p.c. non-cumulative income certificates of Rs. 100/- each, carrying preferential claim to repayment of capital and repayable by annual drawing. The Ramnugger Cane and Sugar Co., Ltd. has raised Rs. 6 lakhs by Convertible Notes of Rs. 1,000 each at $2\frac{1}{2}$ p.c., issued at a discount of 4 p.c. and repayable at a premium of 56 p.c. on 31st May, 1950. In a winding-up or in failure to pay interest or otherwise to comply with the terms and conditions on which these notes were issued, they shall be liable to be repaid at a premium of 4 p.c., if repaid on or before 31st May, 1942. In the event of these being repayable after 31st May, 1942, but before 31st May, 1950, the same will be repaid at a premium of 4 p.c. plus an additional 1 p.c. for every completed period of 3 months as from 31st May, 1942. At any time on or after 1st June, 1942 the holder of any note shall have the option to require the company to issue to him or his nominee such number of ordinary shares of Rs. 10/- each at par as would be equivalent in nominal amount to the sum at which his note would be repayable, if it had fallen due for repayment on the date of the exercise of his option, the ordinary shares thus issued ranking *pari passu* with the existing ordinary shares in respect of subsequent financial year. One more instance of shares falling in the miscellaneous group is that of medical ordinary shares issued by the Bengal Chemical and Pharmaceutical Works Ltd. These shares are issuable to Registered Medical Practitioners only and will be issued at a premium the amount of which being determined from time to time by the Directors. Transfer is restricted for the first ten years after the first issue to other such practitioners. Any person becoming entitled to these shares in consequence of the death or insolvency of the registered holder thereof, shall be entitled to register himself in respect of such shares, subject to the provisions of article 26 of the company. These shares will rank *pari passu* with ordinary shares.

We have discussed above shares from two standpoints—from that of capital structure and that of dividend and other rights. In order to complete the picture, we must add one more classification, *viz.*, from the standpoint of the method of transferring them. From this standpoint a three-fold classification may be made into registered, bearer and inscribed securities. The implication of bearer securities is clear enough.

The transfer is effected in this case by the seller merely by the handing over of the certificate to the prospective customer. Obviously it is very much to the advantage of the holder, provided of course that the market for that class of securities is wide enough. Besides, it does away with all formalities. But no less important is the disadvantage from which it suffers, *viz.*, that the dividends have to be claimed by the holder. In case of registered securities, transfer is effected by a deed, compulsorily in case of a statutory company, and may be in case of a registered company according as the articles of association allow not or allow transfer of shares executed under hand. In case of an inscribed security, transfer is effected not in the form of a separate deed but by writing in a register kept for the purpose. Usually the register is kept at the bank, the procedure of transfer being as follows: When the holder disposes of his holdings, it is necessary that he or his duly appointed representative should go to the bank and sign an entry of the transfer.

Shares of American and Canadian Companies change hands in a way that combines the principal features of bearer and registered securities. These are transferrable, not by a separate deed, but by endorsement on share certificates. Although there is space for inserting the name of the transferee on the certificate, yet it is left blank. This is purposely done, particularly if the certificate is registered in a "good name", *i.e.*, in the name of a good institution, firm or bank, the object being to maintain a good market for them so that they may be sold at any time according to the wishes of the owner. But when this procedure is adopted, it is not possible for the concern to know as to who the real owner is to whom dividend is to be sent. What is done therefore is that dividend is forwarded not to the real holder but to the registered one, whether real or not, and it is necessary for the real holder to put in a claim for it from the registered holder.

Another type of shares which have recently come into use is that issued at a discount. It is a recognised principle of the capital structure of a company that it should not pay any dividend out of its capital, except under special circumstances, and that the share capital shall be kept intact. As a corollary it was accepted that the issue of shares at a discount was injurious and was therefore prohibited. In England the legal

prohibition came right upto the year 1929 when it was relaxed, though not abolished, to a certain extent, and certain safeguards and restrictions are imposed, in case shares are issued at a discount, some of the safeguards being as follows: The shares issued at a discount must be of a class already issued. No share can be issued at a discount within one year of the company becoming entitled to commence business and even after that it must be duly authorised by resolution passed at general meeting of shareholders and sanctioned by the court. Every balance sheet issued by the company is to show how much discount on shares remains to be written off at the date when the balance sheet is issued. In India also the underlying principle of the capital structure of the company is theoretically the same as that already mentioned. In practice however undercapitalisation is a very common feature in most, and over-capitalisation in few, concerns in this country and the history of the development of the companies in this country shows that alteration of capital has been a very common feature of their capital structure. Whatever that may be, the issue of shares at a discount was not permitted before 15th January, 1937, except in the case of sale or re-issue of forfeited shares. From that date however a company can, subject to the provisions of Section 105A of the Act, issue, at a discount, shares of a class already issued, if such issue is authorised by a resolution passed in general meeting of the company and sanctioned by the court. The maximum rate of discount should be clearly specified, but in no case should it exceed 10 p.c. At least one year should have elapsed since the date at which the company could commence business before it can issue shares at a discount and must be issued within six months after the date of its being sanctioned by the court, or within such extended time as the court might allow. Particulars as to the discount granted or so much of the discount as has not been written off at the date of the issue of a prospectus or balance-sheet of the company must be contained in the prospectus and also in the balance sheet.

Issue of Debentures.

Unlike the share capital, debentures represent the debt of the company. In India the debenture capital is small and is

mainly in the hands of institutions like banking and other companies, the effect being that only a fraction of it is quoted in the Indian markets and the investors therefore are not too much interested in this scrip. Apart from this, the debentures offer comparatively smaller interest to the investor of funds. As it was pointed out by the *Indian Central Banking Enquiry Committee*, there is a class of Indian investors who look for capital appreciation in its investments and that debenture loans with a fixed yield of interest and with no prospect of capital appreciation have therefore no attraction for this class. But at times this unpopularity seems exaggerated, because in case of government, semi-government and municipal loans, although there is negligible prospect of capital appreciation, yet the amount of investment is maximum in them. The unpopularity of debentures is as much theoretical as the exaggerated speculative character of Indian investors. It should not be taken as a denial of the existence of speculation in Indian market, sometimes of the worst type; but that is no peculiarity of the Indian investor alone but is to be found more or less everywhere. Nay, the opposite tendency is more predominant in this country. As it was pointed out by the Calcutta Stock Exchange Association before the *Indian Central Banking Enquiry Committee*, there is at all times a large class of investors which prefers the security offered by sound debentures to the possibility of capital depreciation. Therefore the factor of greater importance is to be found in the nature of security offered.

The importance of debentures as a source of industrial finance is not the same but varies from industry to industry and concern to concern, depending much on the position of the concern in matters of possession of real estate and property. If its real estate and property position is quite healthy and if its earning capacity is fairly stable, it is easier for a concern to raise funds by issuing debentures than when the position is poor and earning fluctuating. This is best illustrated from the fact that the jute industry, partly because of their monopolistic position, and partly because of better standing in the eye of investors, has been most successful in issuing debentures whereas some others like coal companies have scarcely been successful in this matter. In another field, the issue of debentures

tures has proved successful, *viz.*, in railway and tramway companies. True, the chief railway system in India has been financed by debentures issued by the Government of India or the Secretary of State; but the smaller concerns have been able to raise capital by issuing debentures themselves and that too in considerable amount. A rough idea can be had from the number of concerns issuing debentures in different industries from the following:

Industry.			Number of concerns issuing debentures.	
Railways	...	...	...	17
Coal industry	...	..	...	2
Cotton industry	...	...	...	13
Jute industry	...	...	...	21
Tea industry	...	...	...	8
Sugar industry	...	...	...	15
Engineering	...	...	...	8
Miscellaneous	...	...	...	21

Broadly speaking, debentures are of two types—redeemable and irredeemable. The latter class is rare so far as this country is concerned, because it requires that the financial position of the concern issuing debentures must be above all suspicion, for, it is only then that the investors can invest in irredeemable debentures. In case of redeemable debentures, however, the investor's interest is protected in various ways. In the first place, so long as they continue, they are not susceptible to depreciation on account of depression or with changes in the conditions of Indian money market. Secondly, some of them enjoy the advantage of being withdrawn even before their maturity. Thirdly, provision is made in many cases for the repayment of debenture loans, thereby minimising their financial burden on the issuing concern as far as practicable. Thus provision is made for having a "sinking fund or the amortisation fund, expressly created for the purpose of paying off debentures," which "may be utilised annually or at longer intervals to draw debentures by means of a ballot to the extent the accumulated amount will permit, and thus, gradually by the date of maturity most of the debentures

tures are redeemed relieving the company of the interest burden."

Apart from the above two types, there are various other types some of which may be mentioned in brief. Naked or ordinary debenture, as distinguished from mortgage debenture, is issued without any security whereas the latter type is issued with a charge on the undertakings and assets of the company. When the debenture is a fixed one, it is issued with a charge on some fixed immovable property of the company as security. Floating debenture is issued with a floating charge on movable assets of the company for security. Another variety, bearer debenture, is payable to bearer and transferable by mere delivery, whereas in case of registered debentures they are payable to registered holders and the transfer to be registered with the company. But the list is not at all exhaustive and each issue may represent some new feature. Thus most of the debentures of railway companies are, taxable, or taxfree, bearer bonds, repayable at par. The Darjeeling-Himalayan Railway Extension Co., Ltd. has, in addition to bearer bonds, bearer debentures. The Shahdara (Delhi) Saharanpur Light Railway Co., Ltd., has got neither bearer bonds, nor registered debentures, but $4\frac{1}{2}$ p.c. debenture stock. Only in one or two cases are the bonds registered and transferable by deed only, e.g., Katakhal-Lala Bazar Railway Co., Ltd., Tezapore Balipara Tram Co., Ltd. The Oriental Coal Company Ltd., has two types of debentures, first mortgage and second mortgage, both being taxable bearer bonds repayable at par. The Bengal Nagpur Cotton Mills Ltd., has issued 6 p.c. taxable bearer bonds, repayable in whole or in part at a premium of 3 p.c. In the Cawnpore Textiles Ltd., apart from the provision for repayment at a premium of 2 p.c., the company is to set apart in each year, out of the profits, for the repayment of debentures, a sum of Rs. 12,500/- to form a sinking fund. If in any year the profits do not suffice to provide Rs. 12,500/- the deficiency shall be provided from the profits of the succeeding year or years. The Mohini Mills Ltd., has issued bearer bonds at par and repayable at par by yearly instalment from 31st December, 1943 to 31st December, 1949, with the option of redemption in whole or part at any time after 31st December, 1943. Of other concerns in cotton industry issuing

debentures nothing special needs be mentioned. The following are some of the concerns having bonds, bearer or registered: Edward Sassoon Mills, Ltd., Elgin Mills Co., Ltd., Indore Málwa United Mills Ltd., Minerva Mills Ltd., Morarjee Gokuldas Spinning and Weaving Co., Ltd., R. G. Cotton Mills Co., Ltd., Sholapur Spinning and Weaving Co., Ltd., and Simplex Mills Co., Ltd. The jute industry however presents the most outstanding example of successful issue of debentures. Nothing however needs be mentioned about their special characteristics, except in case of the Mahabir Jute Mills Ltd. In the case of this company, there are 7 p.c. taxable bearer bonds of Rs. 500/- each, issued at par and repayable at par on 30th September, 1951, with the option of repayment at par, in whole or part, after 30th September, 1941, on six months' notice. If this option is not exercised within a year from the aforesaid date, the company will not be entitled to exercise option before 30th September, 1946. In case of redeeming part of the debentures during this option, the particular debentures to be paid off shall be determined by drawings. In the tea industry only a very few concerns have issued debentures, three of which are in the nature of the convertible debenture capital. Comparatively the success attained by the debentures issued is not totally negligible, particularly so when we consider that the industry is a new one, and some of the concerns present special features of their own in matters of debenture issue. Thus the Belsund Sugar Co., Ltd. issued debentures carrying no interest for the first two years but thereafter at the rate of $5\frac{1}{2}$ p.c. per annum (taxable), repayable at par or at the option of the company on 30th September, 1944. The holder of each debenture had the option to subscribe at any time for an allotment of ordinary shares of the aggregate nominal value of Rs. 90/- payable in cash, this option expiring at the end of a certain period. In the case of the Ramnugger Cane and Sugar Co., Ltd., debentures are issued at a discount of Rs. 2/- per cent and are repayable at a premium of Rs. 2/8/- per cent. The Ryam Sugar Co., Ltd., has 7 p.c. taxable bearer bonds. The company shall in each year set apart out of the profits Rs. 18,750 to form a sinking fund for the repayment of debentures. If in any year the profits do not suffice to provide the aforesaid sum, the deficiency

shall be provided out of profits of succeeding year or years. In two other sugar companies, sinking fund provisions for the repayment of debentures have been made. In the engineering industry about eight concerns have issued debentures, of which mention may be made of only one, *viz.*, Indian Iron and Steel Co., Ltd., whose debentures present some special features. There are two classes—first mortgage debentures and convertible second mortgage debentures stock. The first mortgage debentures are redeemable by the operation of a cumulative sinking fund of $1\frac{1}{2}$ p.c. per annum, commencing in 1941, which will be applied in purchases at any price less than par (exclusive of accrued interest) or by annual drawings at par, with the option of redemption in whole or part on any interest date after 31st December, 1951, at a premium of 2 p.c. The holders of convertible second mortgage debentures stocks might at any time upto and including 1943 convert them into fully paid ordinary shares at the rate of one ordinary share of Rs. 10/- for every £1 10s. of convertible stock. All ordinary shares so issued will rank for dividend for the financial year following that current at the date of the exercise of the option and the holder will receive interest on the stock converted in respect of the financial year in which the option is exercised. In the miscellaneous group, a number of concerns have issued debentures, of which mention may be made only of those issued by the Tata Chemicals Ltd. There are three types of bonds—4 p.c. taxable bonds of Rs. 100/-, Rs. 1,000/- and Rs. 10,000/- each. Debentures of Rs. 100/- and/or Rs. 1,000/- each may be consolidated into debentures of Rs. 1,000/- and Rs. 10,000/- each and debentures of Rs. 100/- and Rs. 1,000/- each. A debenture holder may exercise one of the following alternative options in respect of each unit of Rs. 100/- each held by him: (a) between 1st January, 1943 to exchange the unit for 8 ordinary shares of Rs. 10/- each fully paid up; (b) between 1st January, 1944 and 30th June, 1944, on payment of Rs. 8/- in cash, to exchange the unit for 8 ordinary shares of Rs. 10/- each, fully paid up; and (c) between 1st January 1945 and 30th June, 1945, on payment of Rs. 10/- in cash, to exchange the unit for 6 ordinary shares of Rs. 10/- each fully paid up. Otherwise, they are repayable at par on 15th January, 1952, with the option of repayment in

whole or in part at par on or after 15th January, 1948 on 6 months' notice.

Like preference shares, debentures also constitute a financial burden on the issuing concern and must therefore be strictly limited to the earning capacity. For, "constant interest credit which does not share in business losses, *i.e.*, bonds, mortgages and short-term loans, become a danger to the existence of all legal forms of industrial enterprise; for, several years in depression will eat away the capital-stock if interest payments have to be continued." Nay, even in normal years, too much dependence on borrowed funds is unfavourable to the interest of ordinary shareholders whose dividends are proportionately reduced. Even the price of the shares of a concern depending too much on debentures is unfavourably affected. Hence it is necessary to take resort to debentures only ultimately and that too strictly within the earning capacity of the concern.

Debentures in India are mainly of two types from the standpoint of transferability, *viz.*, bearer bonds and bonds transferable by endorsement only, of which the former are more popular. Registered debentures transferable by deed alone are not very common, though not altogether absent. The reason for this is that the debenture-holders are for less formality in matters of transfers. The debentures are redeemable generally at par and at times at a slight premium and are always backed by a cumulative sinking fund.

Need for well-organised agency for Industrial Finance.

The need for a well-organised agency of Industrial Finance in this country has been expressed from time to time. The drawbacks of the existing machinery are too well-known to need emphasis. It is well-known that the existing banking system has not as yet been able to provide necessary facilities of industrial finance. The overcautious policy of these banks has been responsible for this state of affairs. It was expected that the establishment of the Reserve Bank of India would be a step forward. But unlike the Bank of England, the Reserve Bank of India so far has not shown any tendency to come up to the situation and its policy strictly follows the lines of

orthodox banking principle. The case for a separate Industrial Corporation was considered and put forward by the *Central Banking Enquiry Committee*. But so far nothing has emerged out of that recommendation. The difficulties in the way are at times over-emphasized. It is pointed out that as a preliminary step towards the establishment of industrial bank in this country, there should be the development of ordinary deposit banking. Really speaking, the connection between the two lines of development is almost non-existent. If for the sake of argument it is accepted that the development of deposit banking must precede the development of industrial bank, even then it must be said that the war time development of deposit banking has gone a long way in this matter. In fact, the subject of industrial finance has assumed importance in recent times, after the cessation of hostilities. In Britain, already two finance corporations have been started for financing small and large industries. In this country, in their statement on Industrial Policy the Government announced that they were considering the question of starting an Industrial Investment Corporation or an institution of similar type. In certain quarters, apprehension prevails that in this country no experiment should be made in mixed banking and therefore the banks should not participate in any scheme for long-term finance. While the dangers of mixed banking are well-known, it is too short-sighted a policy to keep the banking system out of the schemes of industrial finance. If the banks keep their short and long term investments entirely separate and if the latter is met out of the fund created out of the profits of the bank, the evils of mixed banking need not manifest. The fact is that the Indian banking system has sufficiently developed during the years of 2nd World War. To keep it entirely out of the field of industrial finance would be too short sighted a policy.

Conclusion

We have considered above the different methods of industrial finance as prevalent in this country. But we have made no distinction between capital raised inside the country and capital invested in our industries by foreigners who retain

ownership and control over them. The problem of external capital assumed importance at the time of the enquiry by the *Fiscal Commission* when it was pointed out that the investment of foreign capital inside this country would nullify any measure intended to grant protection. "Protection would attract capital from abroad and with the capitalist would come the technical expert and the trained organiser of modern industrial undertaking.....The educated Indian would play but a small part; and he would in course of time realise that the protective duties mainly served to enable Europeans to exploit the country."

The foreign investments in India differ from foreign investments made in other countries of the East. For her industrial development Japan resorted to foreign loans but she never allowed foreign capitalism to enter into Japan. The position of China is different. She also raised foreign loans but because of her defaults foreign investments feel rather shy of this country. India's case however comes in between the two. Unlike China, she has found it convenient to raise foreign loans, but unlike Japan—and this is the weakest feature of her economy—she has allowed foreign capitalism to come inside the country.

Foreign capitalism in India is not only to be found in Indian industries, but also, and even more predominantly, in the field of banking, insurance, Railways, Tramways, Ports, and shipping as also in the foreign trade of this country. Even in the industry which is regarded as a national industry, I mean, cotton textile industry, according to some estimates, even there over 20 per cent. of the capital is in British hands. Foreign capitalism in India is not to be found in the same degree in all industries or firms, but it varies in degree of ownership and control. Thus for instance, although the jute industry is the outstanding instance of an industry promoted, controlled and financed by British companies, "yet at present some 60 per cent. of the capital is Indian-owned." The same is true of concerns like the Titaghur Paper Mills, Calcutta, which although *prima facie* appear as foreign are now owned by a majority of Indian share-holders. In some cases, although the concern was originally non-Indian, it has now come practically in the hands of the Indians, e.g., the Martin Com-

pany coming in the hands of the Mukerjees. In some industries, e.g., the match industry, it is a monopoly of non-Indians. Thus the West India Match Co., is run with Swedish capital and under Swedish control. Even a large proportion of shares of Indian concerns is owned by this company. The company also controls the supply of match machinery through the Match Manufacturing Supply Company. The same is also true of the soap and engineering industries. Even in case of many concerns where "the capital and control are predominantly Indian, the technical management may be largely in foreign hands, as was the case at first in the cotton and steel industries."

It is very difficult to state accurately the exact amount of foreign capital invested in India. For, no adequate figures for the same are available. The mixed type of ownership makes the compilation all the more difficult. According to an estimate made by the British Associated Chamber of Commerce in 1933, the total British investment in India was about £1,000 million, including the sterling debt of the Government. According to a recent estimate by the *Financial Times*, the total British investment in India in 1936 was £616 millions, including the foreign obligations of the Government. Now that the sterling debt of the Government has been paid off, according to this estimate, the surviving British investments in India will be about £240 millions.

The evils of foreign capitalism have been emphasized by Indian economists. They were in particular pointed out before the *External Capital Committee* (1925), which, in part, endorsed the recommendations of the minority of the Fiscal Commission regarding the imposition of certain restrictions. Even foreign observers have been forced to admit that "some of them (i.e., allegations) contain an element of truth and the problem has arisen how to secure for India the advantages without the disadvantages of the continued use of foreign capital." (Hubbard—*Eastern Industrialisation and its Effect on the West*). None of the recommendations, either of the *Fiscal Commission* or of the *External Capital Committee*, however found favour with the Government and the provisions of the Government of India Act, 1935, introduced safeguards for foreign capitalism and definitely tied the hands of the Indian

Ministers, if and when they will be running the administration. The Second World War has led to the development of a situation as a result of which India could have achieved financial independence. The huge sterling balances that have accumulated in England in our favour could have been utilised to pay off the owners of these concerns, as has been done by South Africa, Canada and U. S. A. Each of these countries, by taking advantages of the war time developments, has purchased the British investments in these countries. Thus the British holdings in U. S. A. have been liquidated, some even at a loss, and South Africa acquired the ownership of gold mines and Canada has obtained the British-owned Canadian Securities and Railway Stocks. A similar line of policy would have been helpful to this country as well. But while the Government has paid off its external obligations, yet it has maintained indifference to the question of liquidation of private investments by Britishers in this country. This is a very unsympathetic attitude. The only ground on which foreign capital—to be distinguished from foreign capitalism—may be supported for the country is that India needs huge capital for her industrial development. But if any such development is really to take place, the Indian credit in world market is enough to enable her to raise foreign loans on her own account. The fact that at one stage in her industrial development these foreign investments have played an important part does not make them sacrosanct. The indifference of the Government in this respect indicates that foreign capitalism is to continue in this country for an indefinite period.

Proposed Industrial Finance Corporation

The purpose of establishing the Industrial Finance Corporation has been described as “making medium and long term credits more readily available to industrial concerns in British India. “The share capital of this Corporation will be Rs. 5 crores divided into 2,000 shares of Rs. 25,000 each, being fully paid up. Of this the Central Government and the Reserve Bank will each subscribe 400 shares while as many as 800 shares will be allotted to the scheduled banks, the balance of 400 shares being available for distribution among insurance

companies, investment trusts and other financial institutions in such manner as the Board may think fit having regard however to the desirability of distributing the shares and the voting rights attached thereto as widely as possible. The shares will be guaranteed by the Central Government, as to both the repayment of principal and the payment of dividend at a rate not exceeding $2\frac{1}{2}$ p.c. per annum. The corporation will not be liable to pay income tax or super tax on its income and profits but the dividend paid by it to the share-holders will be liable to these taxes. The surplus profits of the Corporation, after payment of dividend not exceeding 5 per cent. and building up a reserve fund of Rs 5 crores will be payable to the Central Government.

CHAPTER 11

CORPORATION FINANCE AND INVESTMENT PROCEDURE.

Saving and Investment

The subject of saving and investment has assumed very great importance in contemporary economic literature. For, these two in themselves determine not only the level of economic activity but also that of inactivity. The particular phase of the business organisation, *viz.*, trade cycle, is also made to depend on the divergence between these two factors and the rate of interest has been given a very great importance as the chief determinant of these two. But the peculiar thing is that even to this day there is no unanimity regarding the conception of saving and investment and therefore confusion prevails in this part of the discussion.

What is saving after all? and what is investment? The classical writers did not dive deep into the matter. Thus Marshall wrote, "Interest, being the price paid for the use of capital in any market, tends towards an equilibrium level, such that the aggregate demand for capital in that market at that rate of interest is equal to the aggregate stock forthcoming at that rate." In other words, "the rate of interest and the amount of real income devoted to investment tend to be so adjusted that the quantity of real income demanded for investment at that rate of interest, is equal to the quantity offered at that rate; in such wise that there are no demands unsatisfied and no offers declined." (Pigou: *Employment and Equilibrium*). The classical exposition is not sufficiently clear. But it may be taken that in equilibrium, the "aggregate demand for capital," *i.e.*, investment, is equal to the "aggregate stock forthcoming at that rate," *i.e.*, saving. The use of the word "stock" has at times created confusion, for it may mean stock of goods and also stock of money, and the rate of interest may therefore be money rate of interest or real rate of interest. Another reason for confusion has occurred in Marshall from

the fact that "There is no explicit reference to productive capacity as an element affecting the supply of real investment." Even if we take it that there is explicit reference to that effect, the trouble is not yet over in so far as the volume of saving at a given rate of interest depends not merely on the productive power of the community, but on the extent to which the productive power is actually used for investment purposes. Pigou has tried to defend Marshall's position on the ground that Marshall was concerned with long-run tendencies. "Industrial fluctuations were to have been the subject of a later volume, which, to our great misfortune, was never written." But this sort of apology is worse than none; for, our immediate concern in economic studies is with short-run problems. Whatever that may be, it may be inferred that even in classical writings, the equilibrium position has been regarded as one in which savings is equal to investment. But no further effort was made to explain the phenomenon of trade cycle in terms of saving and investment.

Although the distinction between the two was first introduced in economic literature by Ludwig Mises, yet it received scientific expression in Keynes' *Treatise on Money*, in which Keynes, a true devotee of classical tradition, has maintained the equality between saving and investment as the position of equilibrium and a divergence between the two as being a position other than equilibrium. In *General Theory* however Keynes breaks away from classical outlook and seeks to establish a bilateral relation between these two propositions, according to which saving is always equal to investment, thereby making these two "a mere identity or truism." The identity, from practical standpoint seems to be exaggerated. For even in normal circumstances in some cases the exploitation of existing resources may not permit the investment of the entire savings of the community while at the same time the need for exploitation of vast resources may lead to insufficiency of national savings and resort may have to be taken to foreign borrowings. Therefore, to say that saving, meaning the excess of income over consumption expenses, is always equal to investment is not scientifically correct. If however the proposition is taken to mean that that portion of saving which is actually invested is equal to investment, it is however a differ-

ent matter; but to strive to establish the bilateral relation between the two is to carry it to exaggeration.

Saving is usually taken to mean individual saving and the saving of the community is equal to the totality of the savings of the individuals constituting it. Some idea of individual saving in this country has been given in Chapter IX above. In recent years, however, another type of saving has come in to acquire greater importance, *viz.*, corporate saving. Quantitative studies of the magnitude of corporate saving have been made in advanced countries; but so far no such estimate is available for our own. A rough idea of corporate saving in this country may be had from the following figures for the year 1942/43. The figures are never accurate, but only approximate.

Corporations.	Number of concerns considered.	Capital (Lakhs of Rs.)	Reserve (Lakhs of Rs.)
Cotton Industry	73	2,322	836
Banking	17	1,007	1,013
Coal Mining	53	561	202
Jute Industry	60	2,106	896
Tea Industry	121	495	231
Engineering	26	2,035	760

It will be seen from the above list that corporate saving is quite small in this country. Apart from the reserve maintained, some of the concerns maintain "other funds" whose aggregate figure would be much smaller than that of the reserve. Some of the concerns save a portion of their annual income for special purposes, which may be seen from the following table:

Concerns maintaining special funds.	Nature and purpose of the funds.	Amounts available therein.
Buckingham & Carnatic Co., Ltd.	Reserve for taxation.	Rs. 64,80,957
Cawnpore Textile Ltd.	Debenture Sinking Fund.	55,292

Concerns maintaining special funds.	Nature and purpose of the funds.	Amounts available therein.
Dhakeswari Cotton Mills Ltd.	Dividend Equalisation Fund. Preference Share Redemption Fund.	Rs. 2,25,096 3,00,000
Elgin Mills Co., Ltd.	Debenture Sinking Fund.	9,80,862
Lakshmi Cotton Mfg., Co., Ltd.	Building & Machinery Funds.	44,62,137
Minerva Mills Ltd.	Debenture Redemption Fund.	1,00,000
Iata Mills Ltd.	Debenture Redemption Fund.	4,73,275
Central Kurkend Coal Co., Ltd.	Capital Redemption Reserve.	95,000
Adamjee Jute Mills Ltd.	Reserve for Taxation.	2,33,466
Auckland Jute Co., Ltd.	Capital Fund.	16,00,000
Hooghly Mills Co., Ltd.	Reserve for Taxation.	9,66,113
Howrah Mills Co., Ltd.	Reserve for Taxation.	72,77,131
Khardah Co., Ltd.	Reserve for Taxation.	34,25,403
Kinnison Jute Mills Co., Ltd.	Capital Fund.	10,00,000
Naihati Jute Mills Co., Ltd.	Capital Fund.	20,00,000
Northbrook Jute Co., Ltd.	Capital Fund.	4,00,000
Nuddia Jute Co., Ltd.	Reserve for Taxation.	31,50,000
Reliance Jute Mills Co., Ltd.	Reserve for Taxation.	22,25,000
Union Jute Co., Ltd.	Capital Fund.	7,00,000
Gohpur Tea Co., Ltd.	Debenture Redemption Fund.	1,00,000
Kumardhubi Engineering Works Ltd.	Reserve for Bad debts, etc.	38,444

Apart from these sundry reserves, a few concerns maintain a separate depreciation fund. The number of such concerns is not too many. The following table gives some idea.

Industry	Total No. of concerns.	Concerns main- taining Deprecia- tion Fund.	Total amount in Deprecia- tion Fund. Rs.
Cotton	... 73	30	11,65,82,017
Coal	... 53	1	51,40,000
Jute	... 60	1	2,90 591
Tea	... 121	—	—
Engineering	... 26	3	15,43,16,091

So far as corporate saving is concerned, although it is a factor of great importance in the economic life of a country, yet for our present purpose it is of no great importance. For, investment of corporate saving involves no borrowing nor any floatation of shares; it is already in the hands of the concern and it is for the concern to decide as to when, how and to what extent is this saving to be invested. It is only in case of individual saving that special investment procedure is needed and it is to its study that we shall devote ourselves in the present chapter.

Investment Procedure—Corporation's Standpoint.

No economic activity, particularly the corporate one, can be carried on without finance. Therefore, as soon as the idea of floating a concern takes shape in the mind of the promoter or the promoters, a sound and adequate financial plan is to be prepared if the concern is to avoid impending collapse. It has been found that many a corporation has come to grief owing to unwise financial plan. A financial plan is nothing but the "pattern of stocks and bonds" and "it assumes (1) a pre-determination of corporate capital needs; and (2) satisfaction of those needs for capital in such manner as will best serve the long run needs of the corporation." But how is this capital to be attracted?

As soon as the concern is floated and financial plan prepared, the concern issues a prospectus to the public which is, so to speak, an invitation calling upon the members of the public to subscribe to the shares, and debentures, if any, of the concern. Be it noted that a private company cannot issue prospectus and even in case of a public company, no prospectus can be issued to the public until a copy of the same is filed with the Registrar. If the public company does not issue prospectus, it is at least expected that it shall not allot its shares and debentures unless at least a statement in lieu of prospectus is filed. The issue of a prospectus has been regarded as the most important part of establishing a concern. But the abuses connected therewith are at times so serious that it has been necessary to prescribe legal regulation in the interest of the investors. It is true that "all prospectus should be scanned in a spirit of jaundiced criticism and with the most pessimistic readiness to believe that they are specially alluring traps laid by some designing financier to relieve the reader of some of his money." But it is not always possible for many investors to judge for themselves the investment opportunities and may readily be entrapped. Of course, law is not enough to protect those who cannot protect themselves; yet it is necessary in order to compel the promoters to bring to the public as many facts as are necessary for the purpose of the investors. Thus Section 93 of the Indian Companies Act, as amended in 1936, gives in details the contents of a prospectus. As laid down in that section, a prospectus must state:—

"(a) the contents of the memorandum, with the names, descriptions and addresses of the signatories and the number of shares subscribed for by them respectively; and the number of founders or management or deferred shares, if any, and the nature and extent of the interest of the holders in the property and profits of the company and the number of redeemable preference shares intended to be issued within the date or, where no date is fixed, the period of notice required and the proposed method of redemption; and

(b) the numbers of shares fixed by the articles as the qualification of a director and any provision in the articles as to the remuneration of the directors; and

(c) the names, descriptions and addresses of the directors

or proposed directors and of the managers or proposed managers and managing agents or proposed managing agents, if any, and any provision in the articles or in any contract as to the appointment of managers or managing agents and the remuneration payable to them; and

(d) The minimum subscription of which the directors may proceed to allotment, and the amount payable on application and allotment on each share; and in the case of a second or subsequent offer of shares the amount offered for subscription on each previous allotment made within the two preceding years, and the amount actually allotted and the amount paid on the shares so allotted; and

(e) the number and amount of shares and debentures which within the two preceding years have been issued or agreed to be issued, as fully or partly paid-up otherwise than in cash, and in the latter case, the extent to which they are so paid-up, and in either case the consideration for which those shares or debentures have been issued or agreed to be issued; and

(ee) where any issue of shares or debentures is underwritten, the names of the underwriters, and the opinion of the directors that the resources of the underwriters are sufficient to discharge the underwriting obligations; and

(f) the names and addresses of the vendors of any property purchased or acquired by the company or proposed so to be purchased or acquired which is to be paid for wholly or partly out of the proceeds of the issue offered for subscription by the prospectus or the purchase or acquisition of which has not been completed at the date of issue of the prospectus, and the amount payable in cash, shares or debentures to the vendor, and where there is more than one separate vendor or the company is a sub-purchaser, the amount so payable to each vendor; provided that where the vendors or any of them are a firm, the members of the firm shall not be treated as separate vendors; and

(ff) where any property referred to in clause (f) has within the two years preceding the issue of the prospectus been transferred by sale, the amount paid by the purchaser at each such transfer so far as the information is available and, where any such property is a business, the profits accruing from such busi-

ness during each of the three years immediately preceding the issue of the prospectus or during each year of the existence of the business it less than three years so far as the information is available. A balance sheet of the business concerned made up to a date not more than 90 days before the date of the issue of the prospectus shall be appended to the prospectus; and

(g) the amount, if any, paid or payable as purchase-money in cash, shares or debentures, for any such property as aforesaid, specifying the amount, if any, payable for goodwill; and

(h) the amount, if any, paid within the two preceding years or payable, as commission for subscribing or agreeing to subscribe, or procuring or agreeing to procure subscriptions, for any shares in, or debentures of, the company, or as discount in respect of shares issued, showing separately the amount, if any, so paid to the managing agents: provided that it shall not be necessary to state the commission payable to sub-underwriters; and

(i) the amount or estimated amount of preliminary expenses; and

(k) the amount paid within the two preceding years or intended to be paid to any promoter, and the consideration for any such payment; and

(l) the dates of, and parties to, every material contract, including contracts relating to the acquisition of property to which clause (f) applies, and a reasonable time and place at which any material contract or a copy thereof may be inspected: provided that this requirement shall not apply to a contract entered into in the ordinary course of the business carried on or intended to be carried on by the company or to any contract (except a contract appointing or fixing the remuneration of a managing director or managing agent) entered into more than two years before the date of issue of the prospectus; and

(m) the names and addresses of the auditors (if any) of the company; and

(n) full particulars of the nature and extent of the interest, if any, of every director in the promotion of, or in the property proposed to be acquired by, the company, or where the interest of such a director consists in being a partner in a firm, the nature and extent of the interest of the firm, with a

statement of all sums paid or agreed to be paid to him or to the firm in cash or shares or otherwise by any person either to induce him to become, or to qualify him as, a director, or otherwise for services rendered by him or by the firm in connection with the promotion or formation of the company; and

(o) where the company is a company having shares of more than one class, the right of voting at meetings of the company conferred by, and the rights in respect of capital and dividends attached to the several classes of shares respectively and

(p) where the articles of the company impose any restrictions upon the members of the company in respect of the right to attend, speak or vote at meetings of the company or of the right to transfer shares, or upon the directors of the company in respect of their powers of management, the nature and extent of those restrictions."

The above legal provision has been rendered necessary in order that there may not be suppressions and exaggerations and consequent trouble and loss to the investors, in so far as the law can help them. These should not be taken as enough nor can they be such; but they are necessary as a sort of warning to the prospective investors.

Investment Procedure—Investor's Standpoint.

A company has been floated; the members of the public have been invited to supply capital. How would they do that? In other words, how would the prospective investors be the shareholders of a concern? There are various ways by which an investor can come to acquire the shares. In the first place, he can be a shareholder by subscribing to the memorandum of association before it is registered. It is well-known that the memorandum contains a subscription clause and the persons desirous to be formed into a company subscribe their names to it and also the number of shares that each one of them has agreed to purchase. Thus this class of shareholders comes to exist simply by virtue of their subscription to the memorandum and each one of them must take shares direct from the company and pay calls duly made on them. Secondly, membership is also acquired by application. A member of the

public desirous to take shares has to apply for such number of shares as he is desirous to take and he gets them according as the company thinks it possible to allot to him. It is well-known that there is minimum subscription, *i.e.*, the lowest sum that the directors consider necessary for purchase of property, preliminary expenses and working capital, and this must be subscribed before the directors can allot any of the shares. If applications are not received for minimum subscription within a prescribed time limit after the issue of prospectus, all moneys received from applicants must be returned. Failing this, directors make themselves jointly and severally liable to pay the same with interest. When advertised minimum subscription has been received, it rests with the directors to allot to each applicant the number of shares he has applied for or any less number they may decide upon or none at all. Thirdly, membership may be acquired by transfer of shares, something on which has already been said. Fourthly, membership may be acquired by succession or transmission, which must be distinguished from membership acquired by transfer of shares. Transmission takes place on the death of the holder of shares or on his becoming lunatic or bankrupt. In such case, the management and control of the holding passes by law to his lawful representative who henceforth becomes the holder of shares. The fifth type of membership is that by acquiescence, *i.e.*, by allowing his name to be retained on the register of members or otherwise holding himself out or allowing himself to be held out as a member. The liability in such a case arises from the fact that he has given his assent to remain on the register of members even in a case where his name has been improperly entered therein, or even when he is stopped from denying that he is registered with his consent. Of all these types of membership, that one which interests us for the present is the second one, *viz.*, membership by application.

Every investor has got to take two sets of decisions. In the first place, he is to decide what portion of his income he is going to consume and what portion to save. After this first set of decision is taken, it is for the investor to see as to how he should invest his funds. This is rather a delicate question and its determination depends on his psychological make-up. In the second set of decision, he has to take some sub-decisions.

viz., whether the prospective investor is ready to undertake risk or not, as to whether his aim is to profit by capital appreciation and also as to whether he wants to be the proprietor or the creditor of the concern. It is on these sub-decisions that the second set of decision will depend. However rash an investor may be, naturally his desire is to earn profit and to reduce the risk to the minimum. For, in saving a part of his income, one sacrifices the immediate enjoyments for some future benefit. Under these circumstances, no one would like to see his savings evaporate in loss, unless of course it is unforeseen and at the same time unavoidable. One thing must however be noted here, *viz.*, the possibility of capital appreciation conflicts with the ideal of reducing the risk to a minimum. For, just as capital appreciation leads to gain, capital depreciation leads to loss. That is why the most orthodox investment doctrine would prefer to remain on the safest side and discourage speculation by all means. But that is too much and would stop the wheel of commerce. Therefore the investor's ideal should be to undertake reasonable risk, without entering into speculation as such.

Next the investor is to decide as to whether he should be a creditor or a proprietor. The difference between the two positions should not be overlooked. Creditorship arises out of the holding of government and municipal securities and of bonds and debentures of concerns engaged in different fields of productive and distributive business. They earn a fixed rate of interest and are repayable at some fixed future date either at par or at a slight premium according to the terms between the two parties. Proprietorship of a concern arises out of the holding of ordinary shares. As already noted, his claims to profit come last and he is entitled to the remainder after meeting the demands of all other claimants. Undoubtedly this is a speculative position; for the remainder may be nil or a vast sum. In the former case, the ordinary shareholder gets nothing while in the latter he is entitled to fabulous dividends. Besides, this uncertainty is neither immense in all circumstances nor unworthy to be shouldered. It all depends on the nature of the undertaking and at times the ordinary shares may be more safe and more profitable than even the gilt-edged securities. Therefore the decision here is extremely difficult. It

is true that debentures have security and fixed income; but the extent of security may be exaggerated. On the other hand, an ordinary share of a good concern may not have less security, with the added possibility of unlimited income therefrom.

In this country much of the investment has been decided in favour of government loans owing to the peculiar economic policy of the government. According to the calculation of foreign experts, attached to the *Indian Central Banking Enquiry Committee*, the total capital invested in Government, municipal and other local bodies, loans and securities, and in industrial and joint stock companies including deposits with banks and post offices, but excluding the bulk of foreign capital working in India, comes to about Rs. 700 crores; but it must be noted in contradiction to the views of the foreign experts that this investment is neither sufficient to meet the needs of industry and agriculture nor well-distributed among different uses. So far as the agricultural class in this country is concerned, they are hardly solvent enough to invest in normal years, not to speak of bad ones. Those who can afford to invest, land and jewellery offer greater attraction. The salaried and professional section does save and invest; but by their very nature they are unfit to assume big risk and prefer assured income, however small, from their investment and therefore they invest in post office savings banks, postal cash certificates, government securities, etc. The commercial community no doubt invest a part of their saving in industrial securities and debentures; but even they usually prefer short-term deposits or treasury bills, and at times purchase and mortgage of land and building, for investing their funds. This state of affairs, this preference on the part of the members of the public in favour of investment in government securities and in municipal and port trust loans is "partly due to the principle of 'safety first' followed by Indian investors. . . . confidence on the part of the investor in securities of the latter kind (*i.e.*, industrial securities) would have been greater and consequently his willingness to invest in them, if the investor had the knowledge that decisions relating to industrial and fiscal matters rested solely and finally with the government of the country responsible to its legislature. We also consider that the high rates of interest paid on government borrowings

in recent years have been partly responsible for the relative popularity of Government Securities as compared with industrial shares and debentures."

An interesting study in the merits of investment in ordinary shares has been made by Edgar Lawrence Smith in his *Common Stocks as Long-Term Investments*. He has carried on a historical investigation, covering the period from 1866 to the end of the century and the broad results of his analysis are that high grade bonds failed to demonstrate themselves as having been better investment. Smith has carried on about a dozen tests and has found that in every case the investor would get a higher income from shares than from bonds and debentures. Of course, we must admit, as Hartley Withers says, "that diversified lists of common shares in the industries of a country that is enjoying exceptional growth and prosperity give them a margin of advantage over high grade bonds," but that the process of diversification is not sufficient for the elimination of risk. But even then Withers tells us that in a sample enquiry carried on by Gilbert Layton of the *Economist* for the years 1910-25 in six industrial concerns of England, it was found that the aggregate investment in six companies had appreciated by over 50 p.c. and the investor had received a dividend rising from 5.9 to 11.4 and averaging over 9 p.c. Though the investigation is on too small a scale, yet it is interesting and encouraging especially when we consider that the period covers two big events of history—the great war and post-war collapse. "All that has been proved by these investigations is that ordinary shares have advantages which make it impossible to regard them as necessarily so speculative that we ought to feel rather ashamed of possessing them."

So far as this country is concerned, no such test has been carried out. A few remarks would therefore not be out of place. First of all, let us take the Government, municipal and state loans. In case of Government of India Rupee Loans, the major portion of the debt is incurred at $3\frac{1}{2}$ and 3 p.c., while a portion of it carries interest at 5 p.c. Only once, in the year 1936, the rate of interest on Government of India Rupee loans, has been below 3 p.c., viz., $2\frac{3}{4}$ p.c. Therefore 3 p.c. may be taken as the minimum limit at which the Government of India Rupee loans are raised. So far as the Provincial Gov-

ernment loans are concerned, the rate of interest stands as follows:—

Madras.		C. P.		Punjab.	
1937	3 p.c.	1937	3 p.c.	1933	4 p.c.
1938	3 p.c.	1939	3 p.c.	1937	3 p.c.
1939	3 p.c.			1938	3 p.c.
				1939	3 p.c.

N. W. F. P.		U. P.	
		1932	5 p.c.
1937	3 p.c.	1936	3 p.c.
		1937	3 p.c.

The rate of interest on state loans stands as follows:—

Mysore.		Travancore.	
1920	6½ p.c.	1916	5 p.c.
1921	6½ p.c.	1936	3½ p.c.
1930	5 p.c.	Cochin.	
1933	4 p.c.	1933	5 p.c.
1934	3½ p.c.	1936	3½ p.c.

So far as the Bombay Municipal loans are concerned, the highest rate of interest recorded has been 6 p.c. in 1924, 1924-25, and 1930 and the lowest 3 p.c. In case of Calcutta municipal loans also, the highest rate has been 6½ p.c. in 1920, 1921, 1924 and 1925 and the lowest 3 p.c. The Bombay municipal (Improvement Trust) Loans bear interest mainly at 4 p.c.; only in the year of issue, 1926, the highest rate of interest was offered at 6 p.c. The rate of interest on Calcutta Improvement Trust Loans stands as follows:—

1925	6 p.c.	1936	3 p.c.
1929	5½ p.c.	1937	3 p.c.
1934	4 p.c.	1938	3 p.c.
1935	3½ p.c.		

The Bombay Port Trust Loans mostly pay 4 p.c. and 3½

p.c. In case of Calcutta Port Trust Loans, the rate of interest is as follows:—

1910-15 each year	4 p.c.	1927	5 p.c.
1916	5 p.c.	1928	5 p.c.
1921	6 p.c.	1931	4 p.c.
1921	6½ p.c.	1933	3 p.c.
1925	6 p.c.	1935	3¾ p.c.
1926	5½ p.c.	1937	3 p.c.
1926	5 p.c.	1938	3 p.c.

Thus it is clear that most of the above loans carry a rate of interest which is generally 3 to 3½ p.c. and only at times it exceeds that rate. So far as our public companies are concerned, some such figures are essential in order to show the comparative advantage of the two. One thing needs however be said. Absolutely judged, the rate of dividend declared leads us no where; for so far as the new investor goes, he may have to purchase the shares at a price much higher than the face value of the shares and in this case the rate per cent. of the dividend declines. This Capital appreciation is no doubt an advantage to the seller, particularly the original one, in so far as he gets more than he actually paid for them; but they are a loss to the new investor. Therefore, while judging the comparative merits of investment in Government Securities and industrial securities, we shall do so from the standpoint of investor to-day and not from that of the original investor. We shall take note not only of the dividend declared but also of capital appreciation in order to realise the true position. Further, it must be borne in mind that in the present stage of the industrial development of the country it is useless to study each of the industries as a whole. For many firms in every industry stand below margin. A comparative study is only possible when most of the firms are marginal. Therefore, we have selected a few good concerns, at random, in order to show that investment in good concerns is in no way inferior to that in Government Securities. What is therefore assumed on the part of the investor is that he has sufficient knowledge of selecting good concerns before he makes up his mind for investment. Let us first take the case of banking companies,

The rate of dividend declared and the range of price fluctuation stand as follows:—

Name of the Concern.	Value of Shares.	1933 %	1934 %	1935 %	1936 %	1937 %	1938 %	1939 %	1940 %
Allahabad Bank Ltd. { D.R.* P.R.*	Rs. 100	18 327-220	18 375-316	18 400-375	18 398-352	18 388-372	18 392½-380	18 390-380	18 385-300
Bank of Baroda Ltd. { D.R. P.R.	100	10 101½-75½	10 104-82	10 108-92	10 119½-101½	10 119½-109	10 118-105	10 116-88	10 —
Bank of India Ltd. { D.R. P.R.	100	10 107-96	10 122½-104½	11 127-115	11 142-125	11 147-136¾	11 149-137	11 149-118½	11 —
Central Bank of India Ltd. { D.R. P.R.	50	6 26-19½	6 35¾-23½	8 42½-29½	7 37-31	8 36½-29½	9 32½-28½	9 35¾-26	9 —
Indian Bank Ltd. { D.R. P.R.	{ 50 10	12 93-80 19-15¾	14 121½-93 23½-19	13½ 135-121½ 27-23½	10½ 141-129 31½-26¾	10½ 146-128 34-24½	10 129-110 26-23	10 121½-101 24½-19½	— — —
Punjab National Bank Ltd. { D.R. P.R.	100	5 80-55	6 125-80	6 125-96½	6 104-100	6 112-100	6 111-91	6 103-97	— —
Union Bank of India Ltd. { D.R. P.R.	5	5 4-3	5 4½-4¼	5 6½-4½	5 6-5¼	5 5.15/16-5½	5½ 6-5.7/16	5¾ 6.3/16-5½	— —

*D.R.—Dividend Record. P.R.—Price Range.

It will be seen that the investor derives dividend which in most cases is higher than that on Government loans. Besides, the original investor gains because of capital appreciation. Even the subsequent investors have their share in capital appreciation in so far as they purchase and sell securities with market fluctuations, thereby pocketing the difference. Let us take the case of the Allahabad Bank Limited. In the year 1933, one share of the face value of Rs. 100/- was earning 18 per cent. For the new investor however the interest earned would not be so high; for he purchases the share not at its face value but at market value, which on average for the year 1933 is Rs. 273½. Thus by investing Rs. 273½ on a share of the face value of Rs. 100/-, he earns annually a sum of Rs. 18/- i.e., 6.318/547 per cent.

Let us next turn to the insurance companies. We shall consider only two cases where capital appreciation has been very high.

(See Table I on page 355).

The dividend record of other insurance concerns is also not unsatisfactory.

(See Table II on page 355).

Or take the case of concerns in cotton industry. We have noted the case of only some concerns from Bombay whose range of capital appreciation is great.

(See Table on page 356).

The dividend record as shown in page 356 is not very attractive for the new cautious investor. For in many cases it would hardly prove equal to the rate of interest allowed by the Government on Government of India Rupee Loans. But, for a speculative investor, who is more concerned with capital appreciation, investment in the shares of the above concerns is highly attractive in so far as the range of price fluctuation is fairly wide. From this standpoint also investment in industrial shares should prove more attractive. Another very speculative and hence profit earning scrip is the ordinary and deferred shares of the Tata Iron & Steel Co., Ltd. Here the range of capital appreciation is extremely wide. Thus the market price of the 30 rupees deferred and 75 rupees ordinary shares was as follows in the following years. (*Vide page 357*).

		TABLE I					TABLE II				
Name of the Concern.	Value of Shares.	1933	1934	1935	1936	1937	1938	1939			
Empire of India Life Assurance Co., Ltd.	100	{ D.R. 40	23½	23½	17½	17½	17	17 (Dec.)	{ 1200-776½ in Feb. 875-680 in Dec.	700-530	
Oriental Govt. Security Life Assn. Co., Ltd.	200	{ D.R. 75 P.R.	1735-1400	2375-1568	2900-2280	3100-2800	900-600	62½	62½	62½	
			3700-2350	4425-3400	4900-4150	5605-4650	5975-5235	4560-3800	4675-3635		
Name of the Concern.											
Asian Assurance Co., Ltd.		6¼	6¼	10	6¼	6¼	7½	6¼			
Bharat Insurance Co., Ltd.		15	15	15	15	15	15	15			
Bombay Life Assurance Co., Ltd.		8	12	12	12	14	14	14			
Indian Mercantile Insurance Co., Ltd.		12½	12½	12½ + 1¼ Bonus	15	12½ + 1¼ Bonus.	12½ + 1¼ Bonus.	12½ + 2½ Bonus.			
Industrial & Prudential Assurance Co., Ltd.		8½	8½	8½	8½	8½	10.5/2	12½			
Jupiter General Insurance Co., Ltd.		5	5	5	5	—	—	5			
Lakshmi Insurance Co., Ltd.		20	20	20	30	30	30	30			
New India Assurance Co., Ltd.		7½	7.11/12	8½	8½	1937 March	9.1/6	10			
						Dec.					
Vulcan Insurance Co., Ltd.		5	5	5	5	8½	8.8/9	5			

Name of the Concern.	Value of share.	1933	1934	1935	1936	1937	1938	1939
Ahmedabad Advance Mills Ltd.	100 { D.R. P.R.	17 333 $\frac{3}{4}$ 265	15 341 $\frac{1}{2}$ 262 $\frac{1}{2}$	15 316-275	14 307 $\frac{3}{8}$ 271 $\frac{1}{4}$	15 322-273 $\frac{3}{4}$	17 411 $\frac{1}{4}$ 290	8 435-255
Bombay Dyeing & Mfg. Co., Ltd.	250 { D.R. P.R.	10 826 $\frac{1}{4}$ 675	12 950-680	10 965-711 $\frac{1}{4}$	10 802-640	10 1151 $\frac{1}{4}$ 852 $\frac{1}{2}$	Bonus 977 $\frac{1}{2}$ 778 $\frac{3}{4}$	Bonus 1195-696 $\frac{1}{4}$
Central India Spg. Wv. & Mfg. Co., Ltd.	100 { D.R. P.R.	12 389 $\frac{3}{8}$ 226	8 343 $\frac{1}{8}$ 215	8 386 $\frac{1}{2}$ 216 $\frac{1}{4}$	8 297 $\frac{7}{8}$ 163	7 351 $\frac{1}{4}$ 215	11 338 $\frac{3}{4}$ 215	8 268-187
Hindustan Spg. & Wv. Mills Co., Ltd.	1000 { D.R. P.R.	10 1635-1350	7 $\frac{1}{2}$ 1905 1625	7 $\frac{1}{2}$ 1900-1620	7 $\frac{1}{2}$ 1775-1525	7 1750-1605	Bonus 1900-1650	10 1760-1400
Indian Mfg. Co., Ltd.	1000 { D.R. P.R.	10 1557 $\frac{1}{2}$ 1150	7 $\frac{1}{2}$ 1725-1400	7 $\frac{1}{2}$ 1700-1440	6 1500-1205	7 1300-1105	8 1402-1210	10 1335-1220
Kohinoor Mills Co., Ltd.	100 { D.R. P.R.	—	8	8	10	12	Bonus 8+7	Bonus 10+6
Lakshmi Cotton Mfg. Co., Ltd.	250 { D.R. P.R.	10 980-700	10 885-650	5 860-600	5 665-513 $\frac{3}{4}$	5 700-570	8 348 $\frac{3}{4}$ 242 $\frac{1}{2}$	8 655-400
Phoenix Mills Ltd.	100 { D.R. P.R.	10 343 $\frac{1}{4}$ 250	10 315-230	10 332 $\frac{1}{2}$ 270	10 271 $\frac{1}{4}$ 251 $\frac{1}{4}$	10 345-250	10 292 $\frac{1}{2}$ 220	— 330-200
Sholapur Spg. & Wv. Co., Ltd.	1000 { D.R. P.R.	6 3170-1570	6 3420-2800	6 3040-2600	5 2600-2000	— 2575-1775	6 2650-1860	6 3250-1610
Wadeshi Mills Co., Ltd.	— { D.R. P.R.	— 283 $\frac{1}{4}$ 147 $\frac{1}{2}$	4 291 $\frac{1}{4}$ 130 $\frac{7}{8}$	4 328 $\frac{3}{4}$ 126 $\frac{1}{4}$	5 119 $\frac{3}{4}$ 137 $\frac{1}{2}$	6 321 $\frac{1}{4}$ 230	9 252 $\frac{1}{2}$ 178 $\frac{3}{4}$	7 384-185 $\frac{1}{2}$
Vishnu Cotton Mills Ltd.	500 { D.R. P.R.	12 1695-1392 $\frac{1}{2}$	12 1605-1310	10 1605-1262 $\frac{1}{2}$	10 1300-1127 $\frac{1}{2}$	10 1485-1238 $\frac{3}{4}$	12 1350-1155	12 1475-1000

	1933	1934	1935	1936
Deferred	280-132½	228½-164¾	730-202½	720-460
Ordinary	42½-16	57-42½	157½-56½	152-131
	1937	1938	1939	
Deferred	2150-508½	1860-892½	1560-840	
Ordinary	388-147	370-232	334-205	

The object of the above lines has been to bring home the comparative advantage of investment in industrial and other company shares, as compared with that in Government loans. True, from the standpoint of dividend payment many of them offer comparatively less attraction, but dividend payment is not the sole determining criterion in case of most investors. Their greater concern is with capital appreciation. From this standpoint it may safely be concluded that the investors need not apprehend less earning from investment in judiciously selected industrial shares.

The investor has made up his mind to invest his savings in industrial shares. How would he do that? How can he know as to which concern is a sound one? Sometimes he is influenced by his relatives and friends, who may have some direct or indirect connection with some concern. Some are duped by big names on the board of directors. Some in this country are influenced not so much by the directors as by the name of the managing agents. Though playing very important role in the field of investment, these cannot be regarded as factors directly connected with the operation of a concern. In this respect, two documents are of help, first, prospectus and second, balance sheet. The warnings from the orthodox investment experts with regard to both these documents is too well known to need recapitulation. Suffice it to say here that both of them are instruments which may cleverly be manipulated in the selfish interest of those who are in charge of the management of the concern and hence both of them must be analysed in a spirit of criticism. As soon as the prospectus of a concern is published, the prospective investor is to see whether it is valid under the Act, *viz.*, whether a copy of the same has been filed with the Regis-

trar of the Joint Stock Company. The next point to note is whether the capital structure of the concern is top heavy. It has been pointed out previously that if the capital structure contains too much of a financial burden in the shape of preference shares and debentures, it may on the whole be taken as unsatisfactory. For, not to speak of depression, even in normal times it becomes difficult for it to meet these obligations out of profits. According to Hartley Withers, the ordinary capital ought to be at least one-third of the total. If this be not so, the margin of income available after the provision of debenture interest and preference dividend is not likely to be sufficient to give the debenture and preference securities real security. Nor would the ordinary shares be attractive in so far as the investor in these would hardly feel any attraction for them when he finds that the concern has its hands tied in other financial obligations. From that standpoint one-third capital to be ordinary one seems to be too low a figure. Besides, the prospectus should contain the details of all financial obligations already incurred by the concern so that any prospective investor may judge the situation for himself. No less troublesome and misleading is the other document *viz.*, balance sheet. As Withers says, whereas the liabilities give figures which are certain facts, the assets are expressed in figures which are to a certain extent a matter of guesswork. For, much depends on the trade in question. If the trade has a good prospect, the figures on the assets side may be a rough guide; but if the trade has no prospect, then these figures lead us nowhere. The figures are there simply because they should be there; otherwise they have no validity. If some of the assets are actually sold in the market, they will fetch a negligible amount. Again, take the case of a particular factor, *viz.*, goodwill, which appears in every balance-sheet. It is not something concrete and therefore the critic may "open his shoulders and slog" and say that goodwill "has no right to be in any balance sheet at all" but ought to have been written off years ago out of profits;" yet it is there and is calculated on some guesswork. These and a thousand other tactics remove the reality and the balance sheet becomes an obscurity. If prospectus and balance sheet are no good guides, profit and loss account is equally hopeless for the

purpose. There are certain items in the profit and loss account on the debit side, *viz.*, allocation of reserve and funds for the repair and renewal of premises and plant, depreciation in widest sense, bad and doubtful debts, etc., etc., in which the directors have full discretion and a prudent board would err on the side of excessive provision; but an imprudent and fraudulent board is also no rarity and in that case the board either waits "for a more favourable opportunity for making fuller provision" or "deliberately make provision that they know to be insufficient; and so the amount of the profit that is carried to the balance sheet is increased at the expense of efficiency of business and of profits of future years and to the ultimate undoing of the share-holders and the directors themselves." Under these circumstances, there are two organisations which may be of help to the investor, I mean, the Stock Exchange and the Investment Trust.

Investment Intermediary—Stock Exchange

The Stock Exchange is not an investment institution but only an investment intermediary, so to say, a centralised market for the purchase and sale of scrips. It has added to the mobility of capital and made investment flexible in so far as the investor is sure of getting a continuous and open market wherein to purchase and sell shares according to his convenience. The Stock Exchange also enables the investor to know the price of different securities according as they stand every moment. Every change in the situation affecting the finances will be reflected in the price quotations which are determined by the operation of the best financial and business brains and it also reflects the future trend. From the standpoint of the industrial concerns, the stock exchange determines the flow of capital available to a particular industry. For savings will flow in those channels whose securities are held at prestige in the stock market. So far as the new investor is concerned, the listing regulations of the stock exchange are of help; for before dealings can be opened in any particular scrip on the stock exchange, it must meet certain requirements as laid down and therefore the securities of bogus companies scarcely have any entrance. It is of

course true that the stock exchange authorities do not hold themselves responsible for the soundness of the scrip and the investor invests on his own responsibility; but the fact that dealings in a particular scrip is admitted in the stock exchange adds to its prestige and soundness.

In view of the vastness of the country, the few stock exchanges that operate in India are not only inadequate but also unsatisfactory in their operation. In fact, the Stock Exchanges in Bombay and Calcutta are the only two organised Stock Exchanges. At Madras a stock exchange was opened in 1920 but is in moribund condition. There is also a stock exchange at Ahmedabad, the principal securities quoted therein being those of cotton mill concerns in that centre. In 1940 a stock exchange was started at Cawnpore. Some time back a new share market has been inaugurated at Calcutta whose main purpose is to create a market for those shares which are not quoted in the Calcutta Stock Exchange Association.

The Calcutta Stock Exchange Association was constituted in 1908. Before that date dealings were carried on by a few brokers in the open. The Association was incorporated into a limited liability company in 1923 under the Indian Companies Act, with an authorised capital of Rs. 3 lakhs divided into 300 fully paid shares of Rs. 1,000/- each. No member of the Association can hold more than one share. The total number of members including partners and assistants of the members' firms exceeds five hundred. If a person is willing to be a member of the Association he can do so only by purchasing a share from an existing member and must pay an admission fee of Rs. 5,000/-. The main object of the Association is "to facilitate the transaction of business on the Stock Exchange and to make rules and byelaws regulating the mode and conditions in and subject to which the business on the Stock Exchange shall be transacted and the conduct of the persons transacting the same and generally for the good order and Government of members of the Association." The management of the Association is entrusted to a Committee the members of which are elected annually at the general meeting of the shareholders. The Committee, in its turn, appoints Sub-Committees and honorary office-bearers and per-

forms all work on behalf of the Association. The business practice in the Calcutta Stock Exchange differs from that elsewhere in so far as all transactions are carried on cash basis and therefore there are no settlement days as in London or Bombay. After the contract is made, the delivery is due on the second day and most securities are sold under blank transfer. But that does not mean that transactions on the Calcutta Stock Exchange are carried on smoothly. Just the reverse of it and although delivery is due on the second day, yet months sometimes pass before the shares are actually delivered. Besides, there is a long standing grievance against the Calcutta Stock Exchange Association in so far as it admitted the scrips of a few selected concerns. Therefore recently the Stock Exchange Association of Bengal was inaugurated in order to remove the long standing grievance of the very many concerns who had been refused admission by the Calcutta Stock Exchange Association. The newly inaugurated Stock Exchange Association of Bengal "contained many an element which the most progressive Stock Exchange in this country should endeavour to emulate. For instance, it was admitting the joint stock banks and other limited liability financial institutions as members. This, though unknown to other Stock Exchange in India, was nevertheless a common practice and established usage with the progressive stock exchanges in the West." As already noted, the Association has for its main purpose the creation of a market for those shares which are not quoted in the Calcutta Stock Exchange Association and putting a stop to "all unhealthy speculations."

But the oldest Stock Exchange in India is the Bombay Stock Exchange, also known as the Native Share and Stock Brokers' Association or the Share Bazar of Bombay. It started its operation as early as 1840 with a handful of members and had a steady development since that date, not only in the number of members but also in the volume and extent of business transacted. In the boom days of 1917 another stock exchange, called the Bombay Stock Exchange Limited was established in Bombay; it did very little business and has ceased to function for all practical purposes. The Native Shares & Stock Brokers' Association was established with very

many objects some of which were as follows. The Association is to support and protect the character and status of brokers and to further the interest of both brokers and the public dealing in shares, to provide honourable practice and to depress mal-practices and to settle disputes among the members and to decide all questions of usage, custom or courtesy in conducting brokerage business. The membership of the Association is open to a native of India and is also extended to a British subject who has resided in the Bombay Presidency for at least 10 years before he has applied for membership. There are certain restrictions on membership which have been imposed in order to keep up the prestige of the Association. Thus no person who is below the age of 21 is eligible. So also one who is engaged in some other profession and is not ready to give it up on being a member and one who is already a member of any rival Association in Bombay are not eligible to membership. A candidate who seeks admission must be supported by two existing members of not less than 5 years' standing. In the London Stock Exchange, a candidate must not only be recommended by three existing members called sureties, but each of them must engage to pay £500 to the creditors of the candidate in case he is declared a defaulter within four years from the date of his admission. If a candidate has served as a clerk in the Stock Exchange, or the settling room, for four years, with a minimum service in Stock Exchange of three years, two sureties only are required and they are liable for only £300 each. In the London Stock Exchange, a candidate for membership must seek admission through some existing member who is prepared to retire in his favour or from the representatives of a deceased member, the object of this regulation being to put a check on the number of members. In Bombay however the number of members is fixed by a resolution of the Association from time to time. The application for membership in Bombay is placed before the Board of Directors of the Association and it must be supported in the Board by a clear majority of three-fourths of the members before one is given a membership. Thus it seems at first sight that Bombay Stock Exchange has greater degree of elasticity as to the number of members than that enjoyed by London; but it must be admitted that the London

Stock Exchange also retains some elasticity in so far as there is a rule that if the number of members is insufficient for the transaction of business, it may create a number of special rights of nomination and offer them for sale to members of the Stock Exchange at a price not less than £2,000. The entrance fee for a candidate in the Bombay Stock Exchange is Rs. 30,000 and the annual subscription only Rs. 5/-. The card of membership is entirely a personal right enjoyable exclusively by the person to whom it has been granted, and is not a part of his property or estate to be enjoyed by his successor. The use of the card is also exclusively restricted to the member and it cannot be transferred to somebody else, nor can it be assigned or let out or disposed of in any way. It is only the Board of Directors which has the exclusive right to dispose of or deal with the card in any way it thinks fit. The members may carry on business as 'single entrepreneurs, or partnership. But partnership is not allowed in all cases. It is allowed only when it is between members of the Stock Exchange or between a member and some of his nearest relatives who wish to carry on business not in his own name, but in that of the firm. In any case, the Board of Directors should be intimated beforehand in order that it may issue necessary permission. Partnership in any other form is not permissible.

A peep into the Stock Exchange transactions may be of interest. It is well-known that the business on the Stock Exchange is transacted by members, known as brokers. Only in the London Stock Exchange there are two types of members, jobbers and brokers, the former being the specialists or wholesalers of the stock exchange. The brokers are however not specialists but deal in all sorts of securities, although some of them may specialise in particular scrips. They are agents working on behalf of the members of the public, their main function being to carry out the orders of their clients in matters of purchase and sale of shares from and to the jobbers. Thus it is clear that the jobbers deal not with the members of the public but with brokers and other jobbers. Even the interest of these two classes of members differs. The jobbers are not agents but are dealing on their own account and "in a sense, dealing against the

public," for in the Stock Exchange when the jobbers have shares to dispose of, it is to their interest to obtain the highest price; and when they are to purchase, they try to do so at cheapest price available. Not so in case of brokers. They are mere agents working on behalf of their clients and it is their duty to sell dear and buy cheap for them. The necessity of jobbers in the London Stock Exchange is sometimes disputed mainly on the ground that if other Stock Exchange can do without them, why not London. But that is no argument in favour of or against the institution. Suffice it to say here that the London Stock Exchange dealing as it does in a large variety of securities needs the services of specialists. Even in other Stock Exchanges, particularly New York, the necessity for the services of the specialists is being felt in view of the growing extent of their business. The same however is not true of any Stock Exchange in India; for the volume of business is neither so vast nor so varied as to call for the services of specialists for many years to come.

Sometimes for the purpose of share pushing some unauthorised persons or institutions begin to function, which is quite derogatory to the best interests of the concern as well as to that of the investors. These outside brokers and bucket shops, as these are called respectively, are not really authorised to work nor is their working legal. In England the abuses went so far that share hawking was declared illegal by the Companies Act of 1929. Of course, it should not be taken to mean that the working of all outside brokers, though unauthorised, is injurious. The thing is that the outside brokers are not the members of the Stock Exchange and when they have to carry on transactions, they do so as clients of inside brokers. Usually they do—and it is in their interest also—legitimate and straightforward business with the public; but some of them carry on at different times in different places what are known as Bucket shops. "Under the guise of advertiser and guide on a quick and easy road to fortune, they will for their own gain allure overtrustful members of the public into the devious and uncertain paths of speculating with margins. In threading these tangled tracks, the trustful ones are only too likely

to lose the money they take with them, and eventually come out into the open country of disillusionment wiser and sadder for their foolish ventures." The Bucket shop practices are not the same but vary according to circumstances. In England even after they have been declared illegal in 1929, they still persist. Kissan gives the following illustrations of the Bucket shop practices in his *Investment in stocks and shares*. One such clever scheme that has deluded many unwary speculators is to pose as a big adviser through bogus financial newspapers and circulars. Having thus gained some standing as honest advisers in the estimation of a large number of people, they then begin "to recommend worthless shares, often abusing the privileges of the Stock Exchange to create a fictitious activity in the shares at rising prices, while they were all the time unloading the shares on their dupes." Another Bucket shop practice is the so-called "margin" system. The innocent speculator is invited to buy a certain share in the hope of a rise in its market price. The full payment is not to be made; only the margin is demanded, say a margin of 1s. per share. If the share falls by one shilling, more margin is demanded and if it is not paid, the transaction is closed, the speculator thereby losing 1s. per share. With a fine show of integrity, the Bucket shop tries to convince the speculator that its prices can be verified from the official list of marking in the Stock Exchange. But that is nonsense in view of the fact that the price of a share fluctuates so many times in a single day, and the price at which the Bucket shop pretends to have purchased a particular scrip for the speculator is high if not the highest one. The fact remains that the Bucket shop is not buying the shares for the speculator; he is merely piggling with figures and his interest is exactly opposite to that of the speculator. If the speculator is more shrewd to see a profit on his shares, the Bucket shop so manipulates affairs that difficulties are put in the way of his obtaining the profit in cash. In most such cases, he is induced to gamble with this as margin and to do so till the whole of it evaporates. Another Bucket shop practice is based on the instalment principle, the investor paying a certain amount at the outset and the rest over a period of time by instalments, interest

being charged on the unpaid balance. It is natural that some of the investors at least would like to pay up the balance in exchange for shares they intend to purchase; but usually they are refused the possession of shares, exposing the fact that the bucket shop had not bought and had no intention of buying the shares but was merely operating against the investor hoping to make a profit out of his losses. Legal action may however be taken; but it is often the underlings who have to bear the consequences. "The real principals having decamped beyond reach of the law by the time that the blow falls."

But all this is a mere digression. Still we have introduced the above paragraph in order to bring home the fact that apart from the legitimate dealers, there are many illegitimate ones, though all the illegitimate dealers are not misleading and injurious. Yet since it is difficult to read into the intentions of anyone, it is better to be forewarned and safer to deal with legitimate dealers, unless the illegitimate ones are personally known, or recommended by some intimate quarters. Turning next to the actual transaction, the dealings on the Bombay Stock Exchange are of two types: ready and forward. The ready list contains the shares of banks and railway companies, etc. The forward list consists mainly of ordinary shares of industrial concerns. In every ready transaction, the seller must deliver the shares on the seventh day after the date on which the transfer forms are submitted and the buyer must accept and pay for them within the prescribed time. The forward business is settled monthly. Of these seven days, the first one is Comparison Day, when the contracts are compared, *i.e.*, it is a day for issuing memorandum slips by the buying broker to the selling broker showing the number of shares outstanding to be taken delivery of. On the second day the lists are submitted to the clearing house which at present is the Bank of India. For these services the Bank is annually paid a sum of Rs. 55,000. The clearing house is a common agent of the members in settling transactions between them by giving and taking delivery of securities and making and accepting payments for the same and clearing the difference. The clearing house is however in no way responsible for the

genuineness or otherwise of the securities passing through its hands. But it is compulsory for all members to clear through the clearing house all forward bargains in such transactions as are required to be done by the Board of Directors. The third, fourth and fifth days are Days of Delivery of shares. On the third day, which is the first of delivery days, the Directors declare the making up price and buy in and sell out shares against defaulters. The fifth day is the last day to deliver the shares before 1 p.m. to clearing house. On this day, the differences are adjusted and market is closed for the business. The sixth day is the Pay Day when payment is to be made to the clearing house. On the seventh and eighth days the shares are received from the clearing house.

The kind of business transacted in the Bombay Stock Exchange is speculative in nature. Three types of speculators have been found operating—the bull, the bear and the stag. The bull is a speculator who contracts to buy shares in the expectation of being able to sell them at a profit before the day of settlement. Thus his sole objective is not to receive shares but to receive the difference from a rise in prices over and above the purchase price. If his expectations be falsified, he suffers a loss, from which he strives to get rid of by having his account contangoed or carried over to the next account day, only paying the difference between the original purchase price and the contango rate. The bulls are very much active during boom period when they go on buying recklessly which in the end brings collapse. Those bulls who have some sources of information regarding matters affecting market trend are the only ones most sure to make money on the Stock Exchange. The position of the other animal of the Stock Exchange, *viz.*, bear, is just the reverse. He aims to make money by selling securities. He contracts to deliver them at some future date at a price contracted for, and expects for a fall in price by that date so that by the time he is to give delivery, can purchase, if necessary, the securities at a lower price and thus make profit from the difference. In fact, he sells what he does not possess in expectation of a fall in price, no exchange of securities taking place at any stage. Only the figures are balanced against each other and

profit or loss, as the case may be, paid over. The action and interaction of the bear and the bull on the Stock Exchange keep the prices of scrips steady. For, when there is too much buying by the bulls, the prices soar high; in that case the largest scale selling by the bears in order to make profit by selling high produces an opposite effect. Just the reverse during a bear raid, when the action of the bulls keeps the prices from falling too low.

We have already seen that when the expectations of the bull are falsified, he borrows money in order to be in a position to comply with his contract to purchase. The same is true in case of the bear. In order to save himself from some falsified expectation, he "borrows," not money, but securities. These two borrowing operations have their effect on the contango rate. When the borrowing on the part of the bulls is excessive, contango rates are high; just the reverse when borrowing on the part of bears is excessive. Sometimes the place of the contango rate is occupied by what is known as "backwardation" and it takes place when the supply of securities cannot cope with the demand for them. If the bull wants the securities whose supply is inadequate, the seller will be prepared to give some consideration to the buyer. In case of the bear, the case is just the reverse. For here, when there is a preponderance of bears, they instead of receiving a contango rate will have to pay backwardation for not being able to supply the securities.

The stag is however a mild animal, who applies for shares of a new concern or for some new government loans and expects to make a profit by selling them out immediately at a premium. Since he applies for shares, no matter, whether he purchases them or not, his operation is inherently bullish in nature and if he receives an allotment, he strives to sell it out at a premium. If the calculations of the stag regarding premium are false, in that case he cannot make profit nor can he transfer the shares on another shoulder. If no allotment of shares is made in his favour, the stag neither gains nor loses.

For the sake of comparison, let us see how transactions are carried on in London Stock Exchange. In London Stock Exchange, settlement of all transactions that are not specifically

entered into for cash takes place twice a month. Each settlement takes four days which generally are first four weekdays. The first day is contango day, the second ticket or name-day, the third is intermediate day and the fourth is account-day or pay-day. It is well-known that every purchase and sale on the stock exchange is a contract for next settlement. A bull has purchased securities which he never intends to take up and pay for; but if his expectations are falsified, owing to inadequate rise in prices or an actual fall in them, he will sell the securities for the impending settlement and repurchase them for the next, thereby reopening the bull operation for another fifteen days. These two transactions—selling for one settlement and buying for the next—are the work of the contango day. In the case of the bear, the transactions on the contango day are the reverse in nature, *viz.*, to buy back for the impending settlement and sell again for the next. As already noted, the second day is the name or ticket-day. Though the passing of names or tickets is a very complicated operation, yet it is greatly facilitated by the Clearing House or Settlement Department. We have already seen that on the contango day many of the transactions to be settled at the impending settlement are cancelled out; but yet there remain many transactions in which securities are handed over by sellers to buyers in exchange for cash. But since these securities pass through many hands during the account, it becomes extremely cumbrous if all the formalities of the settlement are adhered to. On the second and third days therefore these formalities are reduced by bringing ultimate buyers into touch with ultimate sellers. The fourth day is the account-day or pay-day, on which the buyers of securities must be prepared to pay for them as soon as they are delivered. If the securities are bearer securities, they should be in the broker's hands on account-day. If however they are registered securities, some time is allowed in order to have the necessary transfer process performed.

We have said more than once that the object of the speculator is not so much to purchase the securities as to earn a profit from price differences. Now, it may be asked, how these price differences arise? What are the factors that affect the movement of prices of securities? They are very many and the

prices of securities are likely to fluctuate as a result of a change in any one or more than one of these factors. But it must be said, in brief, that all this is linked up with the psychology of price movements. "The winds that play upon Stock Exchange markets are as varying and inconstant as those that blow upon the ocean. . . . For days, barometrically speaking, the needle will point to 'fair' and trading on the floor of the 'house' will proceed along quiet and uneventful lines. This it will be easy to see is a desirable state of affairs . . . sooner or later, however, the cloud 'little larger than a man's hand' appears to be followed before long by wind and storm. Even before members are quite aware of it, they are in the midst of a veritable squall." The phenomena affecting price changes may be classified into two—normal and abnormal. Among the abnormal factors affecting the prices of securities, mention may be made of trade boom and slump, war, political troubles and other internal disturbances. It is a law of human psychology that people tend to buy when prices are rising, and sell when prices are falling. But that is not sound enough. For, when prices are rising, any increase in demand for securities would all the more accentuate the rise and if the rise be abnormal it is sure to collapse. Just the reverse in times of depression. So also when war, internal disturbance or political conflict is on the headline of the press, prices of securities show downward tendency. Among the normal factors affecting the prices of securities, we may mention favourable and unfavourable rumours, changes in the board of directors, changes in bank rate, declaration of good dividends, issue or redemption of debentures, nature and extent of industrial and trade activity, etc., etc. Sometimes the shares of different concerns are inter-related and changes in the price of one lead to changes in that of another. "The threat of international complications, industrial disturbances, such as strikes and lock-out, reported budget deficiencies and adverse profit returns, have the effect of causing stocks to depreciate in value. On the other hand, the prospects of cheaper money, bonus distributions, larger dividends, better trade conditions, and similar evidences of prosperity, react favourably on security values and it is true to say that every political and economic event throughout the

world which we see reported in the newspapers is also recorded, weighed, and estimated on the stock exchange and is reflected in the marking down or up of the securities affected." (Hore and Carter: *Investing Made Easy*.)

Of all the factors affecting the prices of securities as mentioned in above paragraph, the importance of the bank rate is realised by very few persons. Yet it is one of the most important factors governing not only the prices of securities but also the investment itself. It is common experience that when bank rate is low, prices of stocks and shares tend to rise; for, with low bank rate, the propensity to invest increases. People borrow money from banks for purposes of investment and this naturally is followed by an increased demand for, and rise in the prices of, securities. Just the reverse when Bank rate is high. In this way, the propensity to invest is stabilised at a particular level of the Bank rate which, it may be said, is the position of equilibrium.

Besides the ordinary dealing on the stock exchange, there are other transactions known as Option deals. Of course "Option business is prohibited," by the Rules of the Native Share and Stock Brokers' Association. Yet the underlying principle of the option deal is interesting to study. Be it noted however that option deal is quite common in the Produce Exchanges of India. Since the underlying principle of option deal in both the Exchanges is the same, let us illustrate it from what is to be found in the produce exchanges. The buyer of an option has to pay some money to secure an option to buy or sell during a specified period a specified quantity of produce (shares in case of Stock Exchange) at the current rate. The money is commonly known as Nazrana or Premium. The party which takes the premium is known as the 'eater' (Khanewala or Khanar) and the party which pays the premium is known as the 'applier' (laganewala or laganadar). The buyer of a Teji-(call) option is a bull and if he finds that the price has not risen, he does not demand delivery of the produce (share) purchased by him and foregoes the consideration money paid by him. The buyer of a mandi-(put) option, on the other hand, is a bear and if he finds that prices have not gone down, he keeps quiet and allows the premium paid by him to be forfeited. The buyer of a Teji-Mandi

option secures the right to buy or sell as it suits him. The buyer of a double option is both a bull and a bear and he expects the market to fluctuate appreciably.

Let us illustrate *option deals* for the sake of preciseness. To take up Teji-option first. A pays to B Rs. 10/- for the right to declare himself the purchaser of a certain number of shares by a specified date at a price of say, Rs. 100/-: Suppose that during the currency of the transaction, price rises to Rs. 103/-. A then declares that he will purchase at the agreed price of Rs. 100/- and B has no other alternative than either to give delivery at that price or pay Rs. 3/- to A. In any case A recovers Rs. 3/- and loses Rs. 7. If the market goes up above Rs. 110/-, the surplus is the profit of A. If the market remains stationary or declines, A does not exercise his option and loses his premium. In case of a Mandi-option, A pays to B Rs. 10/- for the right to declare himself a seller by a specified date at a specified price of, say Rs. 100/-. If the market falls to Rs. 95/- and if A decides to exercise his option to sell, B has either to take delivery at Rs. 100/- or pay the difference, A thereby losing Rs. 5/-. If the market falls below Rs. 90, A is a gainer to the extent of the difference. The Teji-Mandi-Options are merely a combination of two single options and work in the same way as mentioned above, the only difference being that in a double option, the operator buys the right either to purchase or sell so many of shares on a certain date at a certain price and he has to pay the premium twice, instead of once. To illustrate, A pays the premium for the right to declare himself either a seller or a buyer, as may best suit him. Suppose A has paid to B a sum of Rs. 20/ as premium on the basis of an agreed price of Rs. 100/-. In this case A will gain only when prices go above Rs. 120 or below Rs. 80. Any fluctuation between these two limits may only reduce the loss of money paid as premium. How is this amount of premium determined? Obviously enough it depends on the nature of the risk involved. Thus when market is stable, or when the option is a short term one, the premium will be smaller than when the market is unstable or when the option is a long term one.

Enough has been said regarding the functioning of the stock exchange. As already noted, the stock exchange transactions in India, in general, and in Bombay, in particular, are

notorious for their speculative character. In fact, it has been estimated that about 80 to 90 per cent. of the business in Bombay is speculative in character. Thus the stock exchange does not perform the genuine functions entrusted to it so far as this country is concerned. The reason for this is to be found in the situation prevailing after the commencement of the first great war. The war was accompanied by a boom and there was abnormal rise in prices all round. It started first from landed property and cotton and gradually affected the stock exchange scrips. The prices of shares of cotton mills, iron and steel and cement companies that were usually quoted on the Bombay Stock Exchange went higher and higher and the shares of new concerns began to be quoted at a high premium. Corners became very frequent. Before we proceed to examine what steps have been taken to combat the situation, it will not be out of place if we speak a word or two on the corner. A corner is that condition of the stock exchange in which the supply is held by one operator or a clique of operators and in which the other party has contracted to deliver to the operator or the clique what they can only obtain from the operator or the clique. The situation is like this. More shares have been sold than are available for delivery on the settlement day. As the buyers insist on the delivery of shares, the demand for them goes up and prices rise without limit. But since the shares are controlled by the operator or the clique, the seller has to approach them and is compelled to pay any price dictated by them. The evil effects of a corner are cumulative in nature. For when a corner occurs in a particular scrip, the shortseller of that scrip is compelled to sell out other holdings thereby leading to a depression in market conditions, which gradually envelops the whole market. This was the situation after first great war and dissatisfaction against the Bombay Native Share and Stock Brokers' Association was widespread. Therefore, in September, 1923, the Bombay Stock Exchange Enquiry Committee was appointed "to enquire into the constitution, government, customs, practices, rules, regulations and methods of business of the Native Share and Stock Brokers' Association of Bombay, and to investigate any such complaint of the public, and to make any such enquiries with reference to any of the aforesaid matters or any

other matter appertaining to the aforesaid Association as the Committee may deem proper and thereafter with a view to protecting the investing public against the interested or irregular control of business to formulate such definite proposals for the future constitution, control, direction and regulation of the Association as the Committee may deem proper." The majority report made several important recommendations which however were not given effect to. The Association accepted the minority report which did not improve the situation. Again in 1925 there was heavy speculation, to be followed by usual crisis. The situation became critical and the Government threatened with intervention, which came when the Bombay Securities Contractors' Control Bill became Bombay Act No. VIII of 1925. Under this law it became open for any Stock Exchange to apply to Government for recognition and submit for approval rules for the regulation and control of transactions in securities, other than ready delivery contracts and furnish other information. Further, every contract for the purchase and sale of securities other than a ready delivery contract was to be void, unless it was made subject to the above rules and that too between members or through a member of a recognised stock exchange. Following upon the above legal provisions, the object of the Association was amended as follows: "The Association is established to support and protect the character and status of brokers and to further the interests of both brokers and the public dealing in Bombay in stock, shares and like securities and in exchange to promote honourable practices, to discourage and to suppress malpractices, to settle disputes amongst brokers, to decide all questions of usage, customs or courtesy in conducting brokerage business."

Another matter on which the Enquiry Committee, also known as Atlay Committee, made reflections, was with regard to the prevalence of corners in Bombay Stock Exchange which is termed as "the most sinister manifestation of speculation in Bombay." We have already seen how the Bombay Share Bazar was vitiated owing to its prevalence since 1918 and how it was cumulative in its character. The measures adopted by the Board of Directors were regarded as extremely inadequate by the Atlay Committee; nay, it went so far as to

declare that these measures, instead of checking the growth of corners, have encouraged them. The measures adopted by the Board were as follows: The Board passed rules which gave them power to interfere and fix rates in case of an existing or prospective corner in any scrip dealt in on the Bombay Stock Exchange. Whenever the Board declared that a corner has come to exist in a particular scrip, forward dealings in that scrip were prohibited and all unsettled transactions had to be settled at a price determined by the Board. When the Atlay Committee suggested that the action of the Board encouraged corners, the attack was directed against the price fixing regulations. The Board tried to justify its action on the ground that the rules were meant to protect the investing public and that if the Association did not do so, it would be a party to the circulation of falsehood. The Atlay Committee however did not see any force in these arguments. So far as the first justification is concerned, the Committee argued that the genuine investors do not speculate and that if they do so, they would suffer consequences. As regards the second justification, the Committee was of opinion that "It is not for the Association to control the prices of the securities bought and sold in the market for which they provide facilities. It is not incumbent upon the Association to guarantee that the market price approximates to an intrinsic value which none can suggest a satisfactory means of ascertaining. And if this principle be accepted, whenever the market price moves above or below a price deemed for the time being to be intrinsic value, the Committee are party to the circulation of a lie. The absurdity of this contention needs no demonstration." Whatever that may be, it cannot be denied that corners in Bombay Stock Exchange are created by the activities of the bears and that, as the Atlay Committee suggested, the rules framed by the Board of Directors encourage the activity of the bears to an unusual extent because the price fixing regulation limited the amount of their loss. In order to prevent this bear raid, a new Rule 188 has been framed which runs as follows: In case of bear raids or when prices of stocks and shares are unduly depressed in a crisis as a result of reckless short sales, the Board may, by a resolution of not less than one-half of the total number of members of the Board, at a special meeting at

which not less than three-fourths of the total number shall have been present, suspend all forward business for such time as the Board may decide. All transactions before the date of suspension shall be concluded by delivery and payment as usual on the settlement date, unless the Board by a Resolution passed in like manner extends the time for payment of the said shares to the next settlement, or if necessary to the following settlement, and at the same time suspends the selling out rule with respect to all unsettled contracts in such scrip. The liabilities of such intermediaries shall continue during such suspension.

Various other suggestions were put forward before the Atlay Committee with a view to check speculation. One suggestion was that speculation should altogether be checked, while another suggestion favoured cash transactions as in Calcutta and a third was in favour of lowering the high denominations of shares of the companies on the forward list. These were rightly regarded by the Atlay Committee as mere palliatives. According to the Committee the best remedy for corners was that the short sellers should, in the absence of fraud, be left to pay the penalty—that “all contracts entered into for the sale or purchase of shares must be fulfilled by the delivery of the shares or by payment of the purchase price. And if he who has sold shares cannot, on the day of settlement, deliver the shares which he has sold, he must submit to the ordinary procedure of the Exchange, whereby the shares are bought in against him in the open market, unless he can prove to the complete satisfaction of the Committee that he has been the victim of fraud.”

Another investigation into the affairs of the Bombay Stock Exchange was made by the Bombay Stock Exchange Enquiry Committee, also known as the Morrison Committee, in 1936. The terms of reference were that the Committee was to investigate and report on the organisation and methods of the working of the Bombay Share Bazar and to consider whether any modifications are desirable in the interest of the investing public and to make recommendations. The Committee submitted its unanimous report in which it recommended various measures to check speculation. In the first place, it recommended the limitation of the powers of the directors and

increase in the powers of the Government. Thus the directors were given only the following powers of interruption in the natural course of business: (a) Power to suspend the buying in rule with the previous consent of the Government; (b) Power to suspend short selling with the previous consent of the Government; and (c) power to close the market for 24 hours and even for a longer period with the previous consent of the Government. Secondly, the Committee proposed a system of margins for carrying over a transaction. The fixing of the actual marginal proportion was to be determined by the Exchange in consultation with the Government, but it was hinted by the Committee that a percentage of 10 p.c. or 15 p.c. on the initial bargain price might meet the case, or if it was not possible to introduce a system of margins, the settlements should be made fortnightly, as is the practice in London. Thirdly, the capital sum involved in each transaction should be stated clearly on the contract note so that the speculator may know exactly the extent of his obligation. It has also been suggested by the Committee that the rules in regard to defaulters must be strengthened in the following lines: (a) any compromise to avoid default should be prohibited; (b) a defaulter's property outside the stock exchange must be made available to the association for the benefit of his creditors; and (c) a defaulter should never be admitted as a member if his default is due to his speculation. Be it noted that under the new Rules and Regulations of the Bombay Stock Exchange sanctioned by the Government, the Board of Directors is, save as otherwise provided in the Rules, prohibited from fixing prices at which shares shall or shall not be bought and sold, and from fixing rates at which or above which or below which sales or purchases in shares shall or shall not be made. Under the Rules the Board may intervene only when such intervention is necessary for public interest when a particular scrip has been cornered by an operator or syndicate, and cannot be obtained for delivery except at prices arbitrarily dictated. The Board may also intervene when they are satisfied that there is a fraud connected with dealings in the scrip. When the Board intervenes, it fixes the price in the manner prescribed in the rules and all unsettled contracts in the scrip must be finally settled and concluded at this price. Any intervention by the

Board must be recorded, along with circumstances and reasons for intervention, in the proceedings of the Board and a copy of the minutes must be forwarded to the Government of Bombay.

Need for Investment Trust.

The inadequacy and speculative character of the stock exchange transactions in this country have been sufficiently emphasized in the above section. Even when the stock exchanges direct the flow of capital to industry by providing a market for the purchase and sale of recognised stocks, shares and debentures, they only touch a small proportion of the savers directly, particularly so in India where investment is restricted to a small class of urban savers. This is not all. In this country there are no such institutions as investment banks or investment trusts. The present banking system, with its conservative outlook, is utterly unsuited for the purpose nor do the banks tender advice to their clients about investments, for if they do so, they feel themselves to be morally responsible if the investment proves unprofitable. Money lending, however, absorbs a considerable proportion of small savings; but although since the passing of Moneylenders Acts in some provinces, this flow has to some extent dried out, yet the new course of small savings is not so much towards industrial investment as towards investment in government loans of smaller denomination and in gold and silver. It is essential that these small savings should be pooled together through some specialised organisation and directed into fruitful channels. The resources of small savers are neither sufficient nor is their information adequate so as to enable them to have a diversified investment with their small savings. Hence the need for investment trust, particularly at this stage when small savings have multiplied, which, if not done, would lead to their waste.

Not only does the investment trust facilitate investment by small savers but it also enables the small savings pooled together to be invested in such a way that the risk involved may be the least. It is well-known that the underlying feature of modern business is the assumption of risk which is too large and too varied for the small investor to shoulder. But where

investment takes place through specialised institution, there is every possibility of this risk being reduced to the minimum. The underlying feature of the investment trust organisation is this: It issues shares or bonds for sale among the prospective investors. With the proceeds that they get in this way, they purchase an assortment of securities in various companies, not for control, but only for investment. Out of the interest and dividends received, they pay interest and dividends on their own securities. The success of an investment trust depends on whether the directorate consists of fully qualified men of undoubted standing and repute in the financial world or not.

Before taking up a closer study of investment trust, it must be noted that the investment trust is not the same organisation as investment banker. For, the investment banker buys securities primarily for sale. If the selection is wrong, the investment banker suffers in good-will. For, the payment of dividend or otherwise will not go to the investment banker, but to the holder of the securities. Not so in case of investment trust. For the investment trust purchases securities not for transfer but for holding them, any profit or loss being borne by the trust organisation. All questions of purchase, transfer and sale of securities are to be decided by the directors, of course, sometimes within the prescribed limit. But, even in this case, within the limit they have their discretion. It is of course true that if the investment trust makes a profit, it will add not to the personal benefit of the directors but to that of the shareholders of the investment trust, but even then it must be admitted that the relation of shareholders is an indirect one, while that of the investment trust *vis-a-vis* the concerns in which it has invested is a direct one. Not so in case of investment banker. It follows as a corollary from this that while the investment banker is always on the alert to protect its own interests, the investment banker's interest being remote, he is less cautious and his sole interest lies in passing the securities over to somebody else.

The organisation of investment trust is not of the same type, but different from country to country and even within the same country. Roughly speaking, investment trusts are of two types—fixed and discretionary. The fixed trust is an American institution but is not unknown in Europe. It is

also known as unit trust. The underlying principle of a fixed trust is that the securities in which trust funds are invested are fixed in advance by the promoters and no change can be effected in them for a pre-determined period of time, except in case of recapitalisation, consolidation, reorganisation or sale of the property of any of the companies. With additional funds coming in its hands, the trust may purchase additional securities, but cannot sell, and substitution is allowed only in extreme cases. The fixed trust is not an incorporated company but only regulated by a trust deed and the cost of operating such trust is small. Investments by a fixed trust are represented by units and sub-units. Thus it may be laid down in the trust deed that each unit shall represent so many ordinary shares of each of the different companies permitted. To suit the smaller investors, each unit is divided into sub-units. The chief advantage enjoyed by this type of investment trust is that speculation is minimised; but at the same time it must be admitted that since the hands of the management are tied, opportunities for investment in promising new concerns are minimised. For, while the directors of the British investment trust, also known as management trust, can vary the trust's securities at will according as the opportunity presents itself, the fixed trust can only do so in specified circumstances, distributing the proceeds amongst the holders of units and sub-units.

A management trust, as distinguished from the fixed trust, gives the management wide powers so as to enable them to keep on their portfolio at all time those securities which are the best so far as income from them as well as capital appreciation is concerned. This is the English type and is characterised by the following features. The management trust is financed by issuing shares, divided into fairly well divided groups. The funds thus pooled together are then invested in varied securities, bearing in mind the principle of distributing eggs in different baskets. The selection of the securities is the task of the management. Once selected, its function is not over but it has to keep continuous supervision on the investment and has to strive in all respects so as to increase the income of the investors. It must however be remembered that the management or discretionary trust has nothing to do with the management and control of the concerns in which it

has invested its funds. The portfolios of British investment trusts generally contain securities of several hundred different concerns. This is not enough for securing diversification. "Diversification is assured only when definite attention is given to restricting investment in any one security, a single industry, or a related group of industries or a circumscribed geographical area." If everything is invested in different concerns in a single industry or in different lines in a particular locality, that is no diversification. The importance of this aspect of diversification is most often neglected in America, and some investment trusts have gone so far as to limit the purchase of securities to a single industry or even to a single corporation. The same however cannot be said of investment trusts in Britain.

It is interesting to note that the difference between the above two types is one of the degree of confidence reposed in the management. The fixed trust is built on distrust and suspicion. The aim of the discretionary trust is to select best men for management and to entrust them with the money of the savers so that it may be utilised to their best interests. Both these types go to extremes and therefore a *via-media* has been discovered in Limited Management Trust, which, while attempting to relieve the fixed trust of rigidity, does not allow wide discretion to the management as is done in case of a discretionary trust. The type is also known as "supervised" trust. The need for investment trust in India has already been emphasized. It must be admitted that they are almost non-existent and do not touch even a fringe of the problem. So far the following trusts are found operating in this country with the following objects.

Investment Trusts.	Object.
1. Bird Investments, Ltd.	To invest monies subscribed by the shareholders in the shares and debentures of companies particularly those connected with business and industries in which the firm of Bird & Co. and F. W. Heilgers & Co. are interested. The Company also transacts business in general investment, guarantee, loans and underwriting.

Investment Trusts.	Object.
2. General Investment and Trust Co., Ltd.	To invest monies subscribed by the shareholders in the shares of carefully selected companies and in the securities of the Government of India or Municipal or Port Trust debentures and to transact business as capitalists & financial and monetary agents. It also carries on the business of Guarantee Company.
3. Industrial Investment Trust, Ltd.	To invest monies subscribed by the shareholders in the shares of carefully selected companies.
4. Investment and Finance Co., Ltd.	To invest in shares of carefully selected companies, also in securities issued by the Government of India, Provincial Governments, Municipal and Port Trust debentures. They also have power to act as a Guarantee Company and as capitalists, Financial and/or monetary agents.
5. New India Investment Corporation, Ltd.	To invest monies subscribed by the shareholders in carefully selected companies and to transact business as capitalists and financial and monetary agents. It also undertakes underwriting and guarantee business.
6. Star Trading and Investment, Ltd.	Concerned principally with the investment of funds in the purchase and on mortgage of immovable properties and in the purchase of Government and Municipal securities and in stocks and shares of public companies.

Investment Trusts.	Object.
7. Associated Finance and Investment Corporation (Private), Ltd.	Departments of Business:— (1) Investment Consultants, Company promoters, underwriters, dealers and brokers of stocks and shares, (2) short term advancing for business transactions, direct business enterprise, (3) Managing Agents of joint-stock concerns, Representatives of manufacturers; (4) House building and general construction. Only first two of the above functions taken up so far.
8. Hindusthan Investment and Financial Trust, Ltd.	To invest the funds of the Company in shares and securities of carefully selected companies and to carry on business as a General Investment Trust Company.

So far as is known, the above is an exhaustive list of investment trusts operating in India. Some of them have restricted their activities to serving concerns under a particular managing agency, while others are quite new in the field. Most of them have, as their object, the investment of funds in Government, Municipal and Port Trust Securities, and not industrial ones, which though important from the standpoint of the small investors and the investment trust organisation itself is of little use so far as industrial investment is concerned. Leaving aside these, there are no institutions, properly speaking, to sponsor the sale of shares and debentures to the public. Some of the investment trusts have got underwriting function as their objective, but this function is not of much importance in view of the fact that the managing agents supply all necessary finance when they start any enterprise. When new issues are underwritten, this is done practically by stock-broking firms only. In Bengal there have been a few cases in recent years where reputed stock-brokers have underwritten the shares of companies. Thus, for instance, Messrs. Place, Siddons & Gough underwrote a large block of shares of the Indian Malleable Castings, Ltd., Rohtas Industries, Ltd., and

the Ramnugger Cane & Sugar Co., Ltd.; Messrs. Stewart & Co. and Narayandas Khandelwal & Co. underwrote the entire public issue of the Calcutta Safe Deposit Co., Ltd. (c.f. B. C. Ghosh. *A Study of the Indian Money Market*). Owing to the lack of adequate investing organisations and where finances are not provided by Managing Agents, the new concerns have to depend on public issues of shares and debentures. The unpopularity of debentures in this country is too wellknown to need repetition. The shares of the new concerns have therefore to depend on the mercy of the public who, in their turn, have no guide to advise them to direct the flow of their savings in desired channels. Among the other investment intermediaries, mention may be made of insurance companies. But it is peculiar that the securities held are most Government and semi-Government ones. The following table shows the percentage analysis of assets of Indian Life Insurance Companies.

Year.	India Govt. Securities & Indian States Securities.	Port Trust, Improvement Trust and Municipal Securities.	Shares in Indian Cos.	Miscellaneous
1914	59.15	16.08	1.77	23.0
1919	59.71	14.64	2.44	23.21
1925	53.51	17.28	3.34	25.87
1930	41.34	14.88	2.74	41.04
1931	51.61	14.01	4.13	30.25
1935	50.91	10.52	6.20	32.37
1938	52.81	9.06	7.08	31.05

Some of the insurance concerns have in their holding a large number of industrial shares, "but the reason for opposing investment in shares is that if the stock holdings were small, the investment was at the mercy of stock-holders while if the stock investments were larger there was temptation to secure full control, with the result that the company purchasing stock was thus led into active participation in enterprises quite foreign to the purpose for which it was chartered. Further, if we note the fact that insurance business has only

affected a microscopic section of the Indian population, the inadequacy of these investment intermediaries becomes all the more apparent. The broad conclusion arrived at is therefore that neither the investment trusts nor the insurance companies in this country have rendered any appreciable service in matters of industrial investment, that the propensity to save and invest is therefore so low and that there is a huge wastage of small savings that may arise from time to time. If propensity to save and invest is to increase and if India is to make progress in the field of industrialism—which she should do, if possible, in her self-interest—then mere dependence on big savings and utter disregard for the smaller ones should be regarded as suicidal. As a first step towards industrialism, all the national resources, of which small savings constitute a lot, should at once be mobilised by the organisation of suitable institutions for the purpose.

Finally mention may be made of an experiment carried on in Bengal through the organisation of the Industrial Credit Syndicate, established in 1937 at the instance of the Government of Bengal for supplying long term finance to small industries to be started by persons, in particular ex-detenus, trained under the Unemployment Relief Scheme. The Government offered certain special facilities in order to enable the syndicate to make long term advances. But even then the experiment was not much of a success, partly because of the conservative policy and partly because of clash with the Government. The terms offered by the Government indicate that the Syndicate is expected to advance loans upto about Rs. 10 lakhs whereas the amount actually advanced was even less than a lakh. Early in 1942 the agreement between the Syndicate and the Government came to an end because the Syndicate had at a meeting of its shareholders effected a vital change in the under-writing clause of its Articles of Association without prior consultation with, or with the approval of the Government. Be it noted that sound investment does not depend on over-cautiousness, but on a careful selection of concerns in which to invest. Over-cautiousness at times stands in the way of progress.

CHAPTER XII

CORPORATION FINANCE AND ALLIED PROBLEMS.

Capitalisation.

The question of capitalisation is one of the most vexed questions of Corporation Finance. For while it has been considered that a fair capitalisation is beneficial to the interests of the concern, both over-capitalisation and under-capitalisation have been viewed with grave concern, not only from the standpoint of the concern itself but also from that of the public and of the bigger interests of the community. In general, however, excessive capitalisation is more frequent a feature of Corporations than under-capitalisation in advanced industrialised countries and there is a general belief that many of the most serious evils of our economic life are traceable to this factor. From the standpoint of the Corporation itself, over-capitalisation brings down the credit-standing of the concern. "The weakened condition of the Corporation's credit makes difficult the raising of new capital. To offset this weakness, maintenance is starved, depreciation charges, if any are made, are reduced, and other artificial means are used to inflate net earnings in order to make a better showing for the Corporation. Even unearned and unwise dividends are used at times to revive the credit-standing." From the standpoint of the share-holders, stock-watering is equally undesirable. For, the issue of securities for which no cash equivalent has been received results in the sale of a large amount of worthless securities to the uninstructed public, who may have taken them only to find them decline catastrophically in value or to find no customer for them except at a very poor price. Thus "watered stock is subject to market manipulation." From the standpoint of the community at large also, over-capitalisation leads to the payment of dividend on the watered stock, thereby raising the prices of the products supplied by the concern. For, this dividend on the watered stock

also becomes a part of cost. On an honest capitalisation, much lower price is more than enough.

What is over-capitalisation and how does it take place? But in order to know this, we must know what constitutes a fair capitalisation. Be it noted however that a slight degree of over-capitalisation is often imperceptible. Only when it exceeds a certain limit, it can be properly detected and unless adequate measures are taken, it becomes a fruitful cause of much serious evils in economic life. In the words of Mead, "a company is only 'properly' capitalised when the par value of its securities outstanding is equivalent to their market value," any position of difference between the two revealing either over-capitalisation or under capitalisation. Thus when the par value of a share exceeds the market value, the position is one of over-capitalisation. To take a concrete case, if a share worth Rs. 200/- sells at Rs. 150/-, then its capitalisation is Rs. 200,000/-, let us say, but the selling value of the shares, "the tokens and symbols of its capitalisation" is only Rs. 1,50,000/-, the extent of over-capitalisation being 25 per cent. Over-capitalisation in this sense is not an uncommon feature in this country.

There is a second sense in which over-capitalisation takes place. Briefly speaking, it originates from under-capitalisation and is to be found widely prevailing in this country. For, when a concern is under-capitalised, it has to depend on outside sources for finances, which means borrowing in some way or other. This imposes a permanent burden on the concern and the interest of the share-holders suffers in so far as they cannot get adequate return on their investment. Nor is it possible for most of these concerns to make provision, after meeting permanent financial obligations, for depreciation fund, reserve against contingencies, etc. The result is that the value of the shares suffers in the market. From this standpoint over-capitalisation in the second sense may be regarded as a mere corollary of the first. It is interesting to note how many concerns in this country are under-capitalised, thereby causing over-capitalisation in the second sense. The following figures showing increase, decrease, or both, of capital of different concerns in various fields of business will

show to what extent Indian concerns are over-capitalised or under capitalised.

Nature of business	Number of concerns increasing capital (implies under-capitalisation.)	Number of concerns reducing capital (implies over-capitalisation.)	Number of concerns both increasing and reducing capital.
Banking	7	2	—
Coal Industry	11	9	1
Cotton Industry	21	6	3
Jute Industry	23	5	—
Tea Gardens	41	6	4
Sugar Industry	15	1	1
Engineering	8	4	6
Insurance	2	2	—
Miscellaneous	31	12	4

It will be seen that so many concerns were under-capitalised which ultimately brought into existence the evils of under-capitalisation. When the concern is under-capitalised and the profit-earning capacity of a concern limited, the shares suffer and their market price goes below the par value.

There is a third sense in which over-capitalisation may take place. Over-capitalisation is said to exist when the paid-up capital in a concern is much in excess of that which is required for meeting its financial plan. It generally happens that in boom period the capital strength of a concern increases much more than the increase in productive equipment. Even when there is extension in productive machinery during boom period, it takes place at a very high price; and when the boom is over, the actual value of the fixed assets becomes much less than the original purchase price and there arises the necessity of reconstruction of capital structure. The cotton industry of Bombay showed an over-capitalisation of this nature; although it was not quite unknown in other industries as well. Thus in Bombay while the paid-up capital increased, during boom period, by Rs. 23,85,56,62/- or 196.0 per cent., the number of spindles increased by 138918 or

36.8 per cent. and of looms by 29.80 or 61.9 per cent. Thus it is clear that the Bombay industries presented "both aspects of over-investment in a boom period, *i.e.*, capitalisation at inflated values and extensions at the high prices which prevail in such a period." The result was that industries in Bombay were very much depressed. Since 1925, much had been done for improving the situation and by the time the Tariff Board (1932) on Cotton Textiles reported, eleven mills had reduced their capital from Rs. 8.82 crores to Rs. 4.6 crores; eleven more mills, which had undergone reconstruction or sale to new concerns, had incidentally reduced their capital from Rs. 2.52 crores to Rs. 1.30 crores and six more companies with a capital of Rs. 1.46 crores were either in liquidation or had been dismantled. Thus the paid-up capital of 68 mills in 1931 stood at Rs. 13.18 crores as compared with Rs. 18.96 crores, the paid-up capital of 77 mills in 1926. The consequence of this reorganisation was, in the words of the Bombay Mill-owners' Representation to the Tariff Board (1932), "that the disastrous inflation which took place in every industry throughout the world during the hectic days of the boom which followed the conclusion of the war did not overwhelm the Indian Textile industry to the extent of permanently crippling it." Or, again, a company whose capital was originally not necessarily excessive in relation to the value of its assets may become over-capitalised, if, owing to a decline in demand, its productive capacity comes to exceed its need or if its assets are diminished as a result of losses incurred or through depreciation in value due to obsolescence, etc. In the first sense, it is well-known that some of our industries have already exceeded the extent of internal demand, in their productive capacity, in normal years. This is the case of jute, sugar and textile industries. Of course, there is no decline in demand; but if the relation between demand and productive capacity be considered the latter has certainly exceeded the former, unless some external outlet be found for our products. And so far as over-capitalisation in the sense of loss or depreciation of assets is concerned, this is a feature in many units in the old established industries. Even in case of those which have come into existence during the inter-war period, many suffer either due to obsolescence or

depreciation owing to excessive working during war years. If however no rationalisation measures are adopted nor any financial adjustment is made in these cases, owing to the decline in the value of these assets, many of these units will become over-capitalised.

There is another sense in which over-capitalisation may be used. It may be due to the fact that the properties of the business concern have been purchased or built up at too high a price or too much has been spent in meeting preliminary expenses. Or it may be due to a heavy and permanent fall in prices, thereby reducing the value of the properties to a much lower figure than that written in the books of the company. This feature is also very common in India. Many a concern starts with top heavy administration and too much expenses in promotion, thereby incurring a permanent financial obligation. If everything is done according to a preconceived plan, over-capitalisation in this sense may be avoided.

Finally, over-capitalisation may be used to mean stock watering or capitalisation of earnings. Suppose a company pays 25 p.c. on its shares. As a result of these large dividends, the shares of that company offer greater attraction, the demand for them increases and consequently the price of shares of that company goes up from, say, Rs. 100/- to Rs. 250/-. The company is under-capitalised and it is to the interest of the management to water the stock in such a way that the dividend does not remain 25 p.c. but comes down to, say, 10 p.c. This can be done by raising the number of shares from, say, 10,000 to 25,000, and on this capitalisation, the dividend per cent will be 10. But these shares will have to be issued in the form of Bonus shares, without taking any money in exchange for them. For, "water includes all that is put into the property except actual money." Another method of stock watering is to increase the nominal value of the shares from Rs. 100 to Rs. 250, in the above case, thereby reducing dividend rate from 25 p.c. to 10 p.c. Stock watering as a remedial measure against under-capitalisation is beneficial to the interest of the concern. The object of such fictitious additions to capital stock may be either to secure profit by selling new stocks to investors or to conceal regular profits of an undertaking by reducing the nominal rate of dividend. But then too much

stock watering, as is sometimes done by the management in its selfish interest is very harmful. For, on the one hand, it facilitates the "wholesale swindling of the investing public," which believes that the nominal value of a share has some relation to the market value, which in actual fact may not exist; and on the other hand, excessive over-capitalisation encourages mismanagement in so far as 'high dividends even out of capital are declared in order to please the shareholders and maintain the prestige of the concern in public estimation.

Whatever may be the cause of over-capitalisation, its effects are harmful to the interest of business. Let us first of all consider the effect of over-capitalisation on some items of cost, *e.g.*, costs of materials, overhead expenses and wages. So far as the cost of materials is concerned, it is generally affected the least, except when over-capitalisation has been very great, leading to financial stringency and consequent difficulty of purchase on good terms on the part of the concern. But the effects of over-capitalisation on overhead expenses are direct. To take one simple instance, if the assets of the concern are written up to boom values, then, in a period of slump, if the amount set aside for depreciation, which maintains a certain proportion with the value of the assets, continues to be based on their inflated value, that represents a greater item in costs and although this money remains in the funds of the company, yet so far as the cost of production of each unit of the product is concerned, it goes up and hence hampers the competitive efficiency of the concern. If however the assets are not over-capitalised but only the goodwill, in that case the effect is insignificant. Thus the net effect of over-capitalisation on cost is that the latter is increased, with the result that the management strives to reduce it, on the whole, by striking on the weakest cost item, *viz.*, labour cost or wages. In countries where rates of wages are generally fixed for the industry as a whole as a result of negotiation between employers' associations and trade unions, it is very difficult to reduce wages and the particular unit in the industry which is over capitalised continues to suffer. But in those countries, as in ours, where labour is least organised, the ultimate effect of over-capitalisation may present itself as wage-cuts, with consequent labour troubles, a feature in the late twenties in the

cotton textile industry in Bombay which was suffering from over-capitalisation. What will be the effect of over-capitalisation on prices? Naturally, it will increase prices, particularly when a concern happens to be in a monopolistic position. But in case of competition, the over-capitalised concern makes smaller profit or no profit or even may incur loss. The extent of the reduced profit or increased loss depends on the capital structure, according as the company is mainly dependent on share capital or on loans and debentures. In the latter case, since interest on loans and debentures constitute a permanent item in cost the position of the concern becomes all the more helpless, and the concern may be forced to liquidation. The general evil effects of over-capitalisation are tremendous. They not only result in a lowering of profits and hence of dividends, but also lead towards diminution of working capital because of the inability of the concern to save any part of its profits, and to a change in "the minds and policy of the men who run the business," for "they have not freedom in making new departures, in taking risks in undertaking business which will absorb further working capital; they have not the confident self-reliance which success brings."

But a feature of greater importance in Indian business is not over-capitalisation but under-capitalisation from which many a concern suffers. The above table shows the position clearly. Of all industries, the most affected is Tea; next to that, in order of place being Jute, Cotton, Sugar, Coal, Engineering, Banking and Insurance. In fact, it will be no exaggeration if we say that many of these concerns pursue under-capitalisation as a definite policy with a view to increase the rate of return by limiting the share capital, a peculiar feature of Indian business. Most authorities on Corporation finance have favoured financing by share capital. In the words of Mead, "From the standpoint of the advantage of the Corporation, the choice between bonds and stocks has generally favoured stocks. A company without debt is a company that is solvent and solvency is the principal thing. Modern industry, no matter how well protected by supposed monopolistic advantages, is subject to such revolutionary changes in methods and markets that the introduction of fixed interest obligations which carry sinking funds as well,—

another form of fixed charge—should, if possible, and in the absence of weighty advantages in the contrary policy, be avoided.” In India, however, as already noted, the position is different.

This peculiar method of Corporation finance originated first in the cotton industry. We have seen above that in some centres, *e.g.*, Ahmedabad, it was very easy to obtain public deposits at a very low interest. It was therefore quite convenient for the industrialist to pool together resources from different persons. It is this factor that stood in the way of popularisation of shares and debentures. The shares that were issued were purposely restricted, first because the management did not like to offer high return on investments by the members of the public, particularly so when enormous deposits were forthcoming at a nominal rate of interest and second because the management wanted to retain most or as many of the shares as possible in the hands of its own people which becomes impossible if too many shares are issued. It is this peculiar feature of Indian financial system, *viz.*, obtaining deposits, at least in some centres, at nominal rate of interests, which has falsified the contention of experts on Corporation Finance. This type of under-capitalisation is particularly to be found in the case of the Ahmedabad Cotton Mill Companies, which are usually started with only one-fourth of the block capital being raised by issuing shares. The whole of the rest is raised either by one-year deposit or by seven-year deposit, more frequently, one-third of it in the latter type and two-third in the former one.

Though originating in the Cotton Industry, under-capitalisation has affected all industries. Whatever difference there is, is due to the degree of under-capitalisation, the maximum having been reached in the Tea industry. The whole situation was revealed when the *Bengal Provincial Banking Enquiry Committee* was carrying on its investigation. It was found by the *Committee* that those tea gardens which are owned by companies registered in England experienced no difficulty with regard to finance, as they were started in most cases with adequate capital raised from shares. Not so in case of Indian concerns. The latter are owned mostly by the joint-stock companies and a few of them to individual

proprietors. The share capital (or the invested capital, in case of proprietary concern) is quite insufficient to meet the financial needs of the gardens and they have to borrow. Be it noted that the nature of the tea industry demands large capital expenditure at the initial stage over a number of years. It has been calculated that the minimum size of a garden on a commercial scale is 500 acres for which the initial outlay is estimated at Rs. 7½ lakhs. The whole of this heavy expenditure cannot be raised from share capital, and funds are often raised either by charging an admission fee of Rs. 20 or Rs. 25 per share or by insisting on similar contributions under the name of deposits. This insufficiency of funds is not due to difficulty in raising share capital; in fact, it has been admitted by a witness before the *Bengal Provincial Banking Enquiry Committee* that the share capital of a tea company could be subscribed two or three times over and not infrequently are the shares sold at a premium. The existing method of financing and the pursuance of a policy of under-capitalisation seem to be deliberate and at the same time convenient in so far as no interest is paid on deposits or admission fee and they are generally refunded to shareholders from early profits before dividends are paid.

Reconstruction of Corporation

Reconstruction is a step following upon some trouble in the life of a Corporation. When the extent of the trouble goes beyond the possibility of control, failure is the only course. But the interest of the management would be to do its best to maintain the Corporation through reconstruction. The most important form of reconstruction of which mention will be made here is the alteration of capital of the Corporation. But the procedure of reconstruction is full of legal technicalities. Thus the power to alter the capital must be given by the articles of the company and the manner in which the alteration can be effected should also be laid down by the articles. If no such power is given and the manner laid down, the company may, by a special resolution, alter the articles so as to provide for them. Alteration of

capital of a company may be effected in several ways. It may be increased, consolidated, divided or cancelled or the shares into which the capital is divided may be converted. In the previous section we have seen the cases in which the share capital has been increased. This increase may be effected in general meeting by an issue of new shares of such an amount as the company thinks fit, and the resolution sanctioning the increase may direct the manner in which such new shares shall be issued or distributed. Where capital is increased beyond the registered capital, the notice of increase, including the particulars of the classes of shares affected and the conditions, if any, subject to which the new shares are to be issued must be filed with the Registrar within 15 days of the passing of the resolution. Where however the directors decide to increase the paid-up capital by the issue of further shares out of the authorised capital of the company, the law requires that these shares are to be offered to existing members in proportion to the shares held by them. If the offer is not accepted or the time specified expires, the directors may dispose of them in the best manner possible.

Just as a company can increase share capital, it can also reduce it. As in the case of the power to increase, so also in that of power to reduce, share capital must be given by the articles. The capital may be reduced by reducing or extinguishing the liability of members for uncalled capital; or by writing off lost capital, or by paying off capital which is in excess of the wants of the company or in any other way approved by the court. A company may, in pursuance of the power conferred by the articles and in general meeting, consolidate and divide all or any of its share capital into shares of larger amount than the existing shares or convert all or any of the paid-up shares into stock or reconvert stock into paid-up shares of any denomination. A company may also be authorised by the articles to sub-divide the capital into shares of smaller amount than is specified in the memorandum. It must however be noted that the amount remaining unpaid on each new share shall be proportionate to that unpaid on the shares from which the division is made. Similarly a company may cancel any shares which at the date of exercising the power in that behalf have not been

subscribed for or agreed to be subscribed for by any person and diminish the amount of its share capital by the amount of the shares so cancelled.

Above we have considered only the alteration of capital. A company may also reorganise its share capital by altering the rights of holders of different classes of shares. If reorganisation involves the consolidation of shares of different classes or division of shares into shares of different classes and an alteration of the memorandum was necessary, it was to be done by a special resolution confirmed by an order of the court. Any such reorganisation however would not be able to affect any of the rights attached to any class of shares granted by the memorandum; for such purpose, a resolution passed by a majority in number of the share-holders holding three-fourths of the share capital of that class was necessary in addition. To take some sample cases of reorganisation, the issued and subscribed capital of the New Victoria Mills Co., Ltd. was reduced as follows under a reorganisation scheme in 1930:

(1) 550,000, 8 per cent. cumulative preference shares of Rs. 10 each were reduced to 321,000, 6 per cent. cumulative preference shares of Rs. 5 each and 228,900 preference shares were cancelled.

(2) 800,000 ordinary shares of Rs. 10/- each were reduced to Rs. 762,750 ordinary shares of Rs. 2/8/- each and 37,250 ordinary shares were cancelled.

(3) At the time of the reduction of preference interest, all rights to un-paid cumulative dividends were cancelled.

In 1932 the Simplex Mills Co., Ltd. was reconstructed, the main features of the scheme being:

(1) The existing share capital of the company was reduced from Rs. 2,250,000 to Rs. 150,000 by reducing the nominal value of the original 9,000 shares from Rs. 250/- to Rs. 16 $\frac{2}{3}$ each and every three shares so reduced were consolidated into one share of Rs. 50 each, fully paid.

(2) The capital of the company so reduced and consolidated was subsequently increased to Rs. 14,00,000 by the

issue of 25000 new ordinary shares of Rs. 50 each offered in the first instance to original share-holders at par in the proportion of $8 \frac{1}{3}$ new shares for every one Rs. 50/- share held by them.

(3) The amount raised by the issue of new shares was applied to reduce the total indebtedness of the company amounting to Rs. 30 lakhs to Rs. $17\frac{1}{2}$ lakhs.

In August, 1940 under a scheme of reconstruction, the authorised and issued capital of the Craig Jute Mills, Ltd. was reduced by reducing the nominal value of each ordinary share from Rs. 2/8/- to amount -8- and of each preference share from Rs. 100 to Rs. 50. The rate of dividend on preference shares was also reduced from 9 to 5 per cent. per annum and all rights to cumulative dividends unpaid from August, 1929 to January, 1940 were cancelled.

A scheme of reconstruction was effected in the Namburnadi Tea Co., Ltd. in June, 1937 when the authorised capital of the company was reduced from Rs. 1000000 to Rs. 535000 by cancelling 15,000 unissued ordinary shares of Rs. 10 each and by reducing the nominal value of the 45000 issued ordinary shares from Rs. 10 to Rs. 3 each, which were thereafter consolidated into shares of Rs. 10 each. All arrears of the cumulative preferential dividend were cancelled and the holders of all such shares were given in lieu thereof one Income Certificate of Rs. 100 for every 20 preference shares held by them, carrying interest at the rate of 5 per cent per annum payable from profits from 1st January, 1936. The existing 40000 preference shares of Rs. 10 each were converted into 40000 ordinary shares of Rs. 10 each, fully paid-up, ranking for dividend and in all other respects *pari passu* with the existing ordinary shares of the company. Out of the total 3000 debentures of Rs. 100 each, 2000 bonds were cancelled by purchase and by drawing, leaving only 1000 outstanding and the authorised capital was thereafter increased to its present figures by the creation of 46500 new shares of Rs. 10 each, which have not been issued.

The capital of the Britannia Engineering Co., Ltd. was reorganised in July, 1939 as follows:—

(1) By consolidation of 20 shares of Rs. 1/8/- each into one share of Rs. 30 which was thereafter sub-divided into 3 shares of Rs. 10 each.

(2) By creation and issue of 60000 additional shares of Rs. 10 each at par to existing share-holders in the proportion 4 such shares for every one share of Rs. 10 held, ranking for dividend and in all respects *pari passu* with the issued shares of the company.

The above is sufficient in order to give an idea as to what reorganisation of capital of a Corporation means. One thing comes out from above discussion. When a Corporation is in difficulty, no right attached to different types of capital can be regarded as sacred; nay, it is in the interest of the owners of capital to forego some of them rather than see the Corporation meeting an inglorious end.

Depreciation

In this section, we shall speak a few words about depreciation. This item is one of supreme importance in the field of Corporation finance; yet in this country it is one of the neglected factors. Whatever that may be, it is the duty of the well-managed business concerns to make adequate provision, out of their annual income, under the head 'depreciation'. For, no machinery, building or tool is permanent; each of them depreciates either due to use or to non-use. It should not be thought that if they are not used, they will not undergo depreciation. They will undoubtedly depreciate. Over and above that, they may become obsolete, *i.e.*, out of date. It is not physical depreciation but depreciation in business importance when a better rival is available in the market. When competition prevails in a particular field of business, the danger from the standpoint of business concerns arising out of obsolescence is very great; for as soon as some new productive equipment comes into existence, some concern may commence using it, to the utter inconvenience of the competitors who may have either to instal the same equipment or to forego profits or incur losses by producing with

old ones. In case of monopoly, however, the concern need not suffer on account of old equipment in so far as it can keep it in reserve and when the old one is exhausted, it can use the new invention. Of course, there is some loss in this process in so far as the new equipment is not being used at once; but the gain is greater in so far as the old equipment does not become obsolete, thereby proving the whole investment in it a dead loss. But in a "world of monopolies," this sort of accumulation "scrap heap" is a matter of every day occurrence and the society becomes poorer for it. Whatever that may be, this decay in business importance—or "business depreciation" as it is some times called—has assumed very great importance in these days and it is necessary that sufficient safeguards should be taken to guard against losses owing to business depreciation, particularly so when giant concerns, both inland and foreign, threaten to overwhelm the minor ones. Thus it will be seen that the causes of depreciation are fourfold—wear and tear, action of element, change in corporate policy as regards the nature and method to production and obsolescence. Each of these sub-items under depreciation is of great significance and if adequate provision is not made for meeting them, the business concern would all on a sudden be faced with losses.

Depreciation and dividend are the only two items in the balance of net profit and it is the opinion of many authorities on the subject that a generous treatment should be accorded to depreciation, if necessary, at the expense of dividend. It has often been a policy with the directors to satisfy the short-run interest of the share holders and to create attraction for them in their concern. This short sighted policy has led them to declare fat dividends even at the cost of allowance for depreciation. A more mischievous and unsound policy cannot be thought of. "The object of the directors and secretaries ought not to be to pay as high a dividend as possible but to do exactly the reverse. A percentage on the capital paid away in dividend can never be recalled, while one retained in hand is always available." No less unsound is the policy of investing the depreciation fund in the business itself. At first sight this method seems extremely attractive in so far as it "implies a living spirit of enterprise and greater

earning power as long as the business expands in profit as well as in value." But it is not always so. For, if bad trade overtakes business or any other unforeseen contingency arises, this policy of investing money accumulated in depreciation fund would not be available. But if the financial position of a concern is sound enough, there is nothing to say, on principle, at least, either for or against any such policy. According to Hartley Withers, "probably the best policy of all is the judicious mixture of the two, by which part of the depreciation fund is devoted to the expansion of the business and part to the acquisition of securities from which an income may be received whatever may be the ups and downs of the enterprise."

It has already been remarked that one of the most neglected factors of Corporation Finance in India is the utter negligence of depreciation provisions. It must of course be admitted that the better managed concerns, in their own interest must provide for depreciation and those in India do not violate this. But the same is not true of all. Worse still, there is no settled policy in this respect for a particular industry nor even for a single concern. Since it is, in general, made a charge on profits, it has retained the weakness of fluctuating-with profits, which in lean years comes to a very low figure and in crisis to something minus, while depreciation of productive equipment, whether due to wear or tear, or elemental reason, or accident or obsolescence, continues unabated. According to the eminent authorities, since depreciation is a regular process, it must be regarded as an item in cost, at least to the extent of physical depreciation of productive equipment.

On this urgent question of providing for depreciation, some light has been thrown on the situation in cotton industry by the investigation of the *Bombay Textile Labour Enquiry Committee*. The work of the *Committee* was no doubt handicapped owing to the non-availability of any survey of the plants in the various centres of Bombay Presidency. However, from the personal observation the *Committee* was satisfied that "with few exceptions, the machinery and plant are kept in a state of reasonable efficiency. It has given us the following figures regarding the sums spent for repairs and

renewals for the last five years immediately before the enquiry (1938):—

Region	1934	1935	1936	1937	1938
Bombay	13.87 (53)	17.87 (56)	17.45 (57)	23.66 (63)	28.62 (63)
Ahmedabad	11.86 (56)	12.91 (57)	12.95 (58)	16.25 (63)	21.66 (61)
Sholapur	1.32 (5)	1.69 (5)	1.61 (5)	1.33 (5)	1.61 (5)
Gujerat (Excl. Ahmedabad)	0.53 (4)	0.52 (4)	0.52 (5)	0.60 (5)	0.53 (5)
Khandesh	0.57 (4)	0.69 (3)	1.11 (5)	0.95 (4)	0.89 (5)
Maharashtra and Karnatak, (Excl. Sholapur and Khandesh)	1.16 (8)	0.91 (7)	0.70 (7)	0.87 (7)	0.95 (7)

Note: Figures in brackets indicate the number of mills considered.

In Bombay Presidency, in addition to such expenditure on renewals and repairs as stated above, all well-conducted concerns make provisions for depreciation whenever profits are earned, although there is no statutory obligation to provide for the same, its determination being dependent on the discretion of the directors. In this matter, therefore, the only thing by which the directors may be guided is the allowance in respect of depreciation accepted for the assessment of the profits of companies for income tax under the Income Tax Act—the maximum rates being 5 per cent on machinery, $2\frac{1}{2}$ per cent on buildings and $7\frac{1}{2}$ per cent on bleaching and dyeing plants. In fact, however, the amount of such authorised allowance is much less, for no further allowance can be claimed in respect of building, plant and machinery against which cent per cent depreciation has already been allowed. Thus, according to the Report of the Special Tariff Board (1936), “On basis of the actual allowan-

ces granted by the authorities the average debit for depreciation works out to 2 3/4 per cent on the fixed capital expenditure.....instead of the average of 4 per cent which has been used to show the financial position of the Bombay Cotton Mill Industry." In Ahmedabad, "on basis of these allowances the average debit for depreciation works out to 3.86 per cent on the original block value of these mills instead of the overhead average of 4.50 per cent which has been used to show the financial position of the Ahmedabad Mill Industry." According to the Income Tax Amendment Act of 1939, allowance is however to be granted in respect of depreciation, upto a percentage to be prescribed, on the written-down value of the buildings, machinery and plant. Two new provisions have also been introduced by the Amendment of 1939. In the first place, it removes the restriction to six years of the maximum period up to which arrears of depreciation could be carried forward, so that the writing off of the arrears of depreciation can hereafter be spread over a long period. And secondly, when obsolete machinery is sold or discarded, the amount, by which the written-down value of the machinery or plant exceeds the amount for which it is actually sold or which is its scrap value, can be treated as an authorised allowance for depreciation. These are legal provisions for the depreciation of assessable profits. The actual determination of dividend is entirely a matter of discretion with the directors, a matter in which the decision is taken on the basis of various factors, such as the extent of profits earned in any one year, the condition of the productive equipment, provision of depreciation in the past, strength of corporate reserve, need or otherwise of declaring some dividend, and similar other factors.

While all this is said, it must be admitted that the provision for depreciation is not of the same nature in all concerns in cotton industry. While it is held by all that depreciation at a minimum rate is held to be the first charge on profits, several mills on one ground or another do not provide for it. Thus the Bombay Textile Labour Enquiry Committee in their Interim Report wrote, "Under-depreciation has been common even with concerns, which have paid dividends, especially in Bombay, and commissions and dividends

have been accorded precedence over depreciation." We have already said that depreciation should be made a part of cost and proper importance should be attached to it. The Tariff Board on Cotton Textiles (1927) did not go so far; they recommended that depreciation should be made a first charge on profits. The idea however did not find favour with the Mill-owners' Associations in Bombay and Ahmedabad, mainly on the ground that any such arrangement in years of lean profits would be difficult. Orthodox authorities on Corporation finance would however suggest that provision for depreciation should be cumulative in nature, the deficiency in one year made good by surplus profits in another. Whatever that may be, the mill-owners of Bombay and Ahmedabad suggest "that it is occasionally expedient to allow small dividends even if full provision for depreciation cannot be made." The following table, adapted and re-arranged from the *Bombay Textile Labour Enquiry Committee Report* (Vol. II), shows the position in the matter of the payment of dividends and commissions by mills which were unable to provide for full depreciation on the income tax basis: —

	1934		1935		1936		1937		1938	
	B	A	B	A	B	A	B	A	B	A
No. of mills supplying information.	59	58	63	58	64	58	66	63	65	60
No. of mills not providing depreciation on income-tax basis.	37	23	42	34	46	29	40	24	36	26
No. of mills paying dividends which have not provided depreciation on income-tax basis.	18	18	19	23	24	19	19	15	15	17
No. of mills charging full agents' commission which have not provided depreciation on income-tax basis.	8	7	19	6	24	6	29	7	28	4

Note: B = Bombay; A = Ahmedabad.

Although no such precise figures are available for other industries, yet the position, so far as provision for depreciation is concerned, is not in any way satisfactory. Thus it was reported by the Tariff Board on Sugar (1938) that "some companies have paid dividends without adequate provision." In the same way, it was revealed in the evidence before Tariff Board on Paper Industry that in some of the paper manufacturing concerns, depreciation charges do not have any relation to block value and that the usual practice in such cases is to put to depreciation a certain amount of profits decided upon in an arbitrary way without any definite relation to the block value. The position in Tata Iron Steel Company seems to be sound, at least, if we are to believe what the Tariff Board reported on it. According to the Tariff Board, ... "The depreciation allowed is calculated on the replacement cost of the plant required for the estimated output. This is a constant figure and consequently the depreciation required can most conveniently be calculated as a constant figure. . . We are aware that the inclusion of the annual allocation of Rs. 78 lakhs in the protective scheme has enabled the Tata Iron & Steel Company to accumulate reserves which have been extremely useful to the Company. . . ." But that does not mean that the same remark applies to the other concerns in iron and steel industry, although the need for the same is nowhere so very great as in this case. For, the iron and steel industry falls in the category of those industries which need sufficient provision for adapting themselves to changes in the methods of manufacture which are quite frequent.

If there is no fixed policy regarding the provision of depreciation, the same is true with regard to its utilisation. In general, there are two methods of utilisation, first, to invest it in the same concern, and second, to invest it in some other concern or in Government or Semi-government securities. Thus two of the leading mills at Sholapur invest the reserve, depreciation and other funds separately while in other centres of Bombay Presidency, they are used in the business of the concerns themselves. In the Tata Iron & Steel industry, the funds are invested in the business of the concern itself. From the standpoint of principle, of course, there may be many

things to say against this practice. For, although "in many cases it so happens that though in the balance sheets, sums appear to have been credited to depreciation account, actually no reserve is found to exist. As a matter of fact the whole depreciation account is nothing but piled up expenditure on repairs, renewals, extensions, etc." But from the standpoint of practice there is nothing to speak either for or against this. Thus, for instance, the position of the Tata Company was thoroughly considered by the Tariff Board which remarked that "we need not insist on any particular method of accounting for the depreciation fund; we see nothing improper in the investment of such funds in the industry itself, in which the management may see their way to earn a higher return than they could outside." The only determining factor should be the soundness of the concern, which being assured, the investment of depreciation provision in the business of the concern itself is in no way prejudicial to the interest of the concern on the one hand and of shareholders on the other. In fact, if the depreciation provisions are continually spent on repairs and renewals, "earnings will be increased by the substitution of superior devices which may cost no more than those which they displace."

There is one more aspect of depreciation, *viz.*, surplus capacity, of which note must be taken before we finish off with this section. Depreciation in the shape of existence of surplus capacity combines two features of depreciation—*viz.*, depreciation due to elemental reasons and that due to obsolescence. In this sense depreciation is a constant feature of our jute industry and is likely to be so, in normal times, with others like sugar. The trouble with regard to this situation is all the more accentuated because of the fact that on most occasions it becomes difficult to provide for depreciation of the whole block. A shortsighted policy at the time of installation of productive equipment is responsible for this state of affairs and may quite easily be avoided if too extensive a plant is not installed without any purpose.

The provision of depreciation has occupied an important place in the discussion of economic theory and therefore it would not be irrelevant if we discuss it briefly. Writers

like Marshall have named it as depreciation and replacement fund and like other costs, it is to be deducted from national dividend before it is distributed among the four factors of production. Keynes has developed an interesting analysis of the same in his General Theory. He distinguishes between three types of depreciation—voluntary and involuntary depreciations and windfall loss. Voluntary depreciation arises out of the actual use of productive equipment in producing a certain output. Involuntary depreciation is however not altogether unforeseen and unexpected: it is due to wastage by obsolescence, destruction by catastrophe or mere passage of time and is termed by Keynes as supplementary cost—entirely different from that used by Marshall. The third type of depreciation, windfall loss, is due to unforeseen changes in market values, exceptional obsolescence or destruction by catastrophe which is both involuntary and—in a broad sense—unforeseen. The concept is important in so far as it is essential for the determination of income—both gross and net. According to Keynes, gross income is to be calculated by deducting from total sales the user cost, i.e., the amounts which the entrepreneur pays out to other entrepreneurs for what he has to purchase from them together with the sacrifice which he incurs by employing the equipment instead of leaving it idle. It must be noted that in the calculation of gross income only voluntary depreciation is taken note of. In finding out the net income, involuntary depreciation—or what Keynes calls supplementary cost—is also to be deducted from total sales. It will be seen that the above analysis is more or less in similar lines with the brief discussion of economic theory summarised in the present paragraph.

Dividend.

The shareholders of a concern while investigating their money have one thing in view, viz., to earn a profit on this investment which at least would not be lower than the rate of interest available for the same fund in the money market. In fact, this market rate of interest is the minimum rate

which they expect to earn. That however does not mean that they will earn this every year out of their investment in stocks and shares. It all depends on the profits earned by the concern. If no profits are earned, the ordinary shareholders get nothing, notwithstanding the fact that if they invested it in money market, they could have earned more. It is at this point that dividend differs from interest. Thus in case of ordinary shares,—not so in case of preference shares—dividend may or may not be paid according as profits are earned or not, and even when profits are earned, the whole of it or a major portion may be removed to the reserve fund by directors at their discretion, but interest on debentures must be paid. Interest is therefore predetermined and fixed; dividend is unknown and uncertain. Yet to a speculative brain, and to one who is ready to undertake risk, investment in rationally selected stocks and shares offers greater interest than the fixed and predetermined rate of interest on debentures. They expect to earn a minimum profit; but their truer expectation is not this much only. For, had it been so, what is the utility of undertaking so much risk and uncertainty? In fact, they expect to earn much more. If the concern earns fabulous profits, it will be too glad to share it in some form or other with the investors. And it is with this end in view that funds are generally invested in stocks and shares.

Before turning to Indian conditions, we must state in brief one or two general principles governing dividend policy. In the first place, the dividend policy is the result of action of various factors. One of the legal restrictions imposed is that dividends should not be declared from capital of the concern thereby maintaining the capital structure. It is to be determined within the limit set by the unappropriated surplus, *i.e.*, surplus after all other demands have been met. It is true that the psychology of the investors demands high dividends. But that is not the only factor. For, apart from legal restrictions there are many other factors which stand in the way of declaring a high dividend. If too high a dividend, quite disproportionate to that declared in other lines, is declared by a particular concern in a particular line, that would signify under-capitalisation and attract funds from

the public, thereby once more reducing dividend to normal. It is also known that in the field of finance corporate savings have come to acquire great importance. Hence if the concern is self-sufficient in matters of finance or at least depends on its own saving for a major part of the investment, it is better not to declare a high dividend but to carry a major portion of the undistributed surplus to the reserve. There are certain industries, *e.g.*, railroads, where profits are earned in the long run only. Over a number of years, no profit can be earned and no dividend declared. In speculative enterprises, a grave uncertainty haunts profits and therefore it is necessary to declare dividend at a very few figures which may be maintained all through the life of the Corporation. No less important is the age of the concern. It is true that a certain dividend becomes essential for a new concern to declare in order to attract the active sympathy of investors; but then where it needs its own earning for its own growth, a cautious dividend policy is commendable. From all these standpoints, the following general principles may be laid down regarding the distribution of profits among shareholders. In the first place, the company newly started should make it a point to pay no dividend or a very nominal dividend over a number of years after the commencement of business. Secondly, it should be the aim of the Company to stabilise the dividend rate and in order to achieve that end, it must first reduce the fluctuation of profits to the minimum, so that a stable dividend policy may be ensured. When all this is done, thirdly, it is for the company to pay out as dividend, in any one year, only a portion of the surplus profits, and not the whole of them, as a matter of financial prudence. How much of these surplus profits are to be paid in dividend is a matter to be considered by the management; no hard and fast rule can be laid down in this respect.

In the above paragraph we have hinted in favour of the stabilisation of dividend rate. Much has been written by authorities on Corporation finance in this matter urging its necessity. Of course the need for stabilisation is not of same urgency in all cases, particularly so in case of "Closed Corporations," *i.e.*, Corporations whose shares are not widely distributed. The urgency for stabilisation is very great in case

of Corporations whose shares are widely distributed. This policy is called for not only from the standpoint of the shareholders but also from that of the Corporation itself. Among the shareholders, of course, two classes must be distinguished—investors and speculators. So far as the speculators are concerned, they are in favour of constant fluctuation in the price of shares. But the interest of genuine investors is altogether different. They desire stability in the income from their investment. This, in its turn, has its effect on the price of securities. For, only those securities will have greater attraction from the investors which earn a stable dividend, and consequently they will have a high and more stable value in the market. If the dividends declared over a number of years are irregularly distributed, *e.g.*, 8, 8, 6, 4, 4, averaging 6 p.c., instead of 6 p.c. per annum over a period of five years, the same security will command a lower price in the former case than in the latter.

From the standpoint of the concern itself, a stable dividend policy is desirable for more than one reason. A Corporation with stable dividend record finds a good reception for any subsequent floatation and that too at a premium. It also improves the borrowing position of the Corporation. A Company on the road to progress will need money at every step for improvements and extensions and is therefore under frequent necessity of selling shares and debentures. The importance of this factor is all the more great in this country because of the fact that the propensity to invest in industrial securities is low and the unpopularity of debentures very great. One method among many for their popularisation is to have a stable dividend record.

The stabilisation of the dividend of a Corporation is so important an affair that even in the years when fat profits are being earned, it is considered proper not to be lenient in dividend policy. Even where the shareholders are given this extra surplus, care is to be taken to create the impression that this extra surplus is a temporary phenomenon. For, if the shareholders come to believe that this extra surplus is something permanent, it becomes disastrous to reduce dividend all on a sudden. Most Corporations in America "plough back" a

part of their earnings. In England however the Corporations are more liberal in allowing the shareholders to have a share in increased profits. Both have their respective advantages and disadvantages. For, while "most English Corporations do not have the opportunity for growth enjoyed by American business enterprises," in America, "large surpluses lead to over-expansion and speculation, resulting from the efforts of Corporation Managers to keep their assets working." Whatever that may be, when a company is to give a share of increased profits to its shareholders, the usual practice, from the standpoint of stabilised dividend policy, is to declare the "regular" dividend and then to give an "extra" dividend, which implies that this is only a temporary affair. If however increased profits are maintained, the extra dividend becomes a regular one.

One of the oft-repeated charges against the dividend policy in India is that the dividend paid is excessive. At times however this charge has proved quite true; but a patient enquiry reveals that the changed policy is due to some changed circumstances and consequently it is essential for being adjusted to changed psychology of the shareholders. The most glaring charge ever made in this country is that against the dividend policy of the Cotton textiles, particularly in Bombay Presidency, in the post-war boom following upon the great war. The matter was pointed out by the Tariff Board of 1927 on cotton textiles which reported that the dividends paid during the boom years upto 1927 were unduly high. In coal mining, the Indian Coal Statistics (1935) shows that out of 66 Coal Companies mentioned in the Calcutta Stock and Share List, 32 declared no dividend, and figures for 9 were not reported; one Company paid 65 p.c.; 2, $22\frac{1}{2}$ p.c.; one 20 p.c.; one $18\frac{3}{4}$ p.c.; one $17\frac{6}{7}$ p.c.; two 15 p.c.; and the remainder between $2\frac{1}{2}$ and 12 p.c. According to the Coal Mining Committee (1937), "the dividends paid by these particular Companies have improved in almost every instance and indicate that whatever may have happened to the property or the machinery or the labour force, the advisability of keeping the shareholders content has not been lost sight of. This may also be due to the fact that, in some cases, the remuneration

of the managing agents depends on the dividends and bonuses paid to shareholders."

These are due to some exceptional circumstances, either due to boom period profit or to the pressure of some interested party, like the managing agents. Otherwise, in general, the dividend declared cannot be regarded as too unreasonable. In this respect however, neither the employer nor the Labourer has been able to take a scientific outlook. Thus, for instance, it has been contended by Labour in Ahmedabad that the payment of dividend by cotton mill companies should be limited to 4 p.c. per annum and that when high profits are earned, they should not be spent on fat dividends, but carried to reserve and depreciation funds and utilised for improving the standard of living of the workers. It has been the contention of the employers that a limitation of dividend would be an unprecedented innovation and would be much resented by shareholders, particularly so when there is no fixed minimum for dividend. While it is true that too fat a dividend is to be deprecated, dividends declared by companies in India in most cases have not been excessive. Even while the Tariff Board on Cotton Textiles (1927) came to the conclusion that the rate of dividend during the boom period following upon the first great war was excessive, yet the Board admitted that this could not be regarded as having contributed to the subsequent depression.

The dividend policy of the cotton textiles was thoroughly examined by the *Bombay Textile Labour Enquiry Committee*. The survey includes not only the cotton textile industry in this country, but the same in other countries, and also the dividend policy of some of the other industries in this country. The broad conclusion arrived at is that "while the cotton textile industry in Bombay has not fared worse than the industry in other countries, the dividends declared in the last few years cannot generally be said to have been excessive. Nor are they high in proportion to the dividends in other centres in the Indian textile industry or in other industries in our country." The comparative figures given by the *Committee* are so instructive that we cannot check the temptation of adapting them here for our purpose.

Number of mills declaring dividend:—

I. Bombay.

Rate of Dividend per cent.	1929	1930	1931	1932	1933	1934	1935	1936	1937	1938
Nil	20	20	20	20	20	22	33	31	28	30
Below 3	—	—	—	1	3	1	8	10	4	3
3 & below 4	1	—	1	—	—	1	2	4	2	1
4 „ „ 5	1	1	1	—	2	8	4	4	6	3
5 „ „ 6	1	—	1	4	—	1	3	2	3	7
6 „ „ 7	—	—	2	2	1	1	2	2	6	5
7 „ „ 8	2	2	—	—	2	2	1	2	3	2
8 „ „ 9	—	—	1	1	—	2	2	—	3	2
9 „ „ 10	—	—	—	—	—	—	—	—	—	1
10 „ „ 12½	6	10	8	7	6	6	7	8	5	9
12½ „ „ 15	—	—	—	—	—	—	—	—	—	1
15 „ „ 17½	2	—	2	2	1	—	—	1	3	1
17½ „ „ 20	—	—	—	—	—	—	—	—	—	—
20 „ „ 25	3	—	—	—	—	—	—	—	—	2
25 „ „ 50	—	—	—	—	—	—	—	—	—	—
50 „ „ 75	—	—	—	—	—	—	—	—	—	—
75 and over	—	—	—	—	—	—	—	—	—	—
unspecified.	—	—	—	—	—	—	1	—	—	—

II. Ahmedabad.

Rate of Dividend per cent.		1929	1930	1931	1932	1933	1934	1935	1936	1937	1938
Nil		13	20	12	10	21	15	26	30	19	20
Below 3		—	—	—	—	—	—	1	—	—	—
3 & below 4		1	—	—	—	—	2	—	3	1	—
4 5		3	1	2	1	1	1	2	2	3	—
5 6		2	2	2	2	5	2	1	4	2	1
6 7		11	11	7	5	12	20	10	11	11	16
7 8		1	2	9	9	4	3	7	3	8	5
8 9		—	2	7	8	1	3	3	3	3	6
9 10		—	1	—	—	—	—	—	—	—	2
10 12½		6	7	7	13	10	5	8	6	9	6
12½ 15		4	1	—	1	1	5	2	—	2	—
15 17½		3	2	4	4	9	9	6	3	2	3
17½ 20		1	2	—	—	2	1	1	—	2	1
20 25		4	6	7	7	2	3	2	1	2	1
25 50		8	4	7	8	2	3	2	2	2	1
50 75		3	3	2	2	1	—	—	—	1	—
75 and over		—	—	—	—	—	—	—	1	—	—
unspecified.		10	7	5	1	3	—	—	—	—	—

III. Other centres—

Rate of Dividend per cent.	U. P.		C. P. & Berar.		Madras.		Bengal.	
	1936	1937	1938	1936	1937	1938	1936	1937
Nil	2	2	1	2	1	1	1	1
3 & below	4	—	—	—	—	—	—	—
4 "	5	—	1	—	—	—	—	—
5 "	6	1	—	1	—	—	—	3
6 "	7	—	—	—	—	1	—	—
7 "	8	—	—	—	1	—	1	—
8 "	9	—	—	1	—	—	—	—
9 "	10	—	—	—	—	—	—	—
10 "	12½	—	1	—	1	1	—	1
12½ "	15	—	—	—	—	—	—	—
15 "	17½	—	—	—	—	—	—	—
17½ "	20	—	—	—	—	—	—	—
20 "	25	1	1	—	—	—	—	—
25 "	50	1	1	—	—	—	—	—
Unspecified	—	—	—	—	—	1	—	—

IV. Dividend paid in textile industry in foreign countries.

Great Britain.		Japan.		U. S. A.	
Period	Rate of Dividend per cent	Year	1st half Year	2nd half Year	No. Dividend of Year per cent. mills.
Year ended June 30th.					
1932	4.4				1917 11.0 60
1933	4.6	1933	10.9	11.4	1920 17.4 60
1934	5.2	1934	13.0	12.1	1921 9.5 60
1935	5.5	1935	12.3	12.6	1929 5.8 58
1936	5.2	1936		12.0	1931 2.7 56
1937	5.2	1937	13.3	12.5	1932 1.7 53
Quarter ended June 30th.					
1938	6.0	1938	13.2	12.3	1933 1.4 50
1939	6.4				1934 3.2 48

V. Other Industries in India—number of mills declaring Dividend.

Rate of Dividend per cent.	Jute.			Sugar.		
	1936	1937	1938	1936	1937	1938.
Nil	10	16	27	7	10	12
Below 3	5	5	10	1	—	2
3 & below 4	3	4	3	—	1	—
4 „ „ 5	—	3	1	—	—	—
5 „ „ 6	3	4	4	3	5	2
6 „ „ 7	3	2	2	—	1	—
7 „ „ 8	5	4	2	2	2	1
8 „ „ 9	2	1	1	1	—	—
9 „ „ 10	—	2	1	—	—	—
10 „ „ 12½	7	6	4	7	6	6
12½ „ „ 15	4	2	3	1	1	2
15 „ „ 17½	1	4	2	3	3	3
17½ „ „ 20	5	2	—	—	—	—
20 „ „ 25	7	4	—	3	—	—
25 „ „ 50	5	1	—	1	—	1

It will be seen that the dividend declared is not excessive when compared between different industries in India or with textile industry in three leading-most countries of the world. Therefore the contention that there must be statutory limitation on the dividend declared is of little use in the present stage of our industrial development. To the utmost this much may be said that in a period of prosperity it is to the interest of the industry itself to build up as much corporate reserve as is feasible so that on the one hand it would lighten the problem of industrial finance in normal times and on the other work as the main support in the dark days of depression.

There is a general impression that the dividend declared by some concerns, like the Tata Iron & Steel Company, is very

high. But this is a wrong impression. As the following table would show, the average annual profit per share has not been very high. Because of the speculative activity in the Tata shares in recent years, particularly in the deferred shares, this impression has got some support. But the nature of the deferred shares should not be confused with that of other shares and if they have shared for long, there is little cause for grumble if they are earning high dividends in times of prosperity. The following table from Adarkar's *Indian Fiscal Policy* is of interest in the context:

Dividend paid by the Tatas.

	1st			2nd			Ordinary.			Deferred.		
	Preference.			Preference.			Ordinary.			Deferred.		
	(Rs. 150)			(Rs. 100)			(Rs. 75)			(Rs. 30.)		
	Rs.	A.	P.	Rs.	A.	P.	Rs.	A.	P.	Rs.	A.	P.
1924-25	5	0	0	0	0	0	0	0	0	0	0	0
1925-26	18	0	0	3	12	4	0	0	0	0	0	0
1926-27	9	0	0	8	0	4	1	0	0	0	0	0
1927-28	9	0	0	7	8	0	0	0	0	0	0	0
1928-29	11	0	0	0	0	0	0	0	0	0	0	0
1929-30	18	0	0	0	0	0	0	0	0	0	0	0
1930-31	9	0	0	2	8	0	0	0	0	0	0	0
1931-32	9	0	0	1	0	0	0	0	0	0	0	0
1932-33	9	0	0	5	0	0	0	0	0	0	0	0
1933-34	9	0	0	15	0	0	0	0	0	0	0	0
1934-35	9	0	0	22	8	0	0	0	0	0	0	0
1935-36	9	0	0	17	8	0	6	0	0	7	8	0
1936-37	9	0	0	15	2	0	10	0	0	36	3	6
1937-38	9	0	0	20	10	0	15	8	0	75	11	3
1938-39	9	0	0	22	2	0	18	0	0	93	10	5
1939-40	9	0	0	7	8	0	25	0	0	143	14	7

The average rate of dividend in Tata Iron & Steel Company comes out as follows:—

(a) Annual average since 1924-25:—

First Preference—6.4%

2nd Preference—8.5%

Ordinary—3.1%

Deferred—3.7%

(b) Annual average since inception and upto 31st March, 1940.

First Preference—6%

2nd Preference—7½%

Ordinary—6.23%

Deferred—10.46%

The question of stabilisation of dividend rate has not altogether been neglected in this country, although it may not have received the same sort of handling as in other countries. Its theoretical importance has been noted in an earlier paragraph. As a matter of practical policy, two sorts of measures have been adopted. In the first place, efforts have been made by the managing agents, particularly the non-Indian ones, to stabilise the rate of dividend. This is the case in jute mills, coal companies, transport companies, tea companies, etc., where the managing agents ensure to the shareholders the same rates of dividend after allowance is made regarding the location, technical conditions, etc. Another and a less successful method is the institution of Dividend Equalisation Fund by some concerns. The object of the fund is to equalise the rate of dividend over years. It will be seen from the following that although a number of concerns has instituted the device, it has not yet been a success. But this much may be said that if properly handled, the device has good prospects for the purpose of stabilisation of dividend rate. The following chart gives the name of the concerns instituting the device and shows the range of dividend fluctuation over a period of a decade:—

Name of the concern instituting Dividend Equalisation Fund.	Range of dividend Fluctuation.
1. Ahmedabad Advance Mills, Ltd. ...	8. & 17 p.c.
2. Bombay Dyeing & Mfg. Co., Ltd. ...	10 & 24 p.c.
3. Central India Spg., Weaving & Mfg. Co., Ltd. ...	7 & 14 p.c.
4. Century Spg. & Mfg. Co., Ltd. ...	5 & 24 p.c.
5. Colaba Land and Mill Co., Ltd. ...	2½ & 7½ p.c.
6. Coorla Spg. & Weaving Co., Ltd. ...	4 & 10 p.c.
7. Dhakeswari Cotton Mills, Ltd. ...	7½ & 10 p.c.
8. Finlay Mills, Ltd. ...	2½ & 10 p.c.
9. Indore Malwa United Mills, Ltd.	No dividend since 1933.
10. Malabar Spg. & Weaving Co., Ltd.	3 & 20 p.c.
11. R. G. Cotton Mills Co., Ltd.	No dividend since 1932
12. Swadcschi Mills, Co., Ltd. ...	4 & 18 p.c.
13. Western India Spg. & Mfg. Co., Ltd. ...	4 & 17 p.c.
14. Union Bank of India, Ltd.	Even dividend rate
15. Burrakur Coal Co., Ltd.	Even dividend rate
16. East India Coal Co., Ltd.	Even dividend rate.
17. Albion Jute Mills Co., Ltd. ...	3 & 12 p.c.
18. Belvedere Jute Mills Co., Ltd. ...	10 & 30 p.c.
19. Budge Budge Jute Mills Co., Ltd.	6 & 35 p.c.
20. Caledonian Jute Mills Co., Ltd. ...	8 & 30 p.c.
21. Dalhousie Jute Co., Ltd. ...	4 & 20 p.c.
22. Delta Jute Mills Co., Ltd. ...	10 & 35 p.c.
23. Empire Jute Co., Ltd. ...	2½ & 15 p.c.
24. Gondalpara Mill ...	2½ & 30 p.c.
25. Hooghly Mills Co., Ltd. ...	10 & 50 p.c.
26. Kamarhatti Co., Ltd. ...	7½ & 35 p.c.
27. Kankinarrah Co., Ltd. ...	7½ & 30 p.c.
28. Kelvin Jute Co., Ltd. ...	10 & 40 p.c.
29. Lawrence Jute Co., Ltd. ...	4 & 25 p.c.
30. Lothian Jute Mills Co., Ltd. ...	3 & 20 p.c.
31. National Co., Ltd. ...	5 & 20 p.c.
32. New Central Jute Mills Co., Ltd. ..	8 & 25 p.c.
33. Northbrook Jute Co., Ltd. ...	5 & 20 p.c.
34. Standard Jute Co., Ltd. ...	4 & 20 p.c.

35. Dehra Dun Tea Co., Ltd.	...	4 & 16	p.c.
36. New Dooars Tea Co., Ltd.	...	10 & 90	p.c.
37. Sungma Tea Co., Ltd.	...	2½ & 7½	p.c.
38. Punjab Sugar Mills Co., Ltd.,	...	6 & 40	p.c.
39. Indian Iron & Steel Co., Ltd.*	...	15 & 35	p.c.
40. Indian Standard Wagon Co., Ltd.*	...	5 & 15	p.c.
41. Jost's Engineering Co., Ltd.	...	5 & 17½	p.c.

*Dividend Adjustment Account and Not Dividend Equalisation Fund.

Thus it will be seen that the device has not yet proved successful. The concerns should, in their own interest, strive to make the dividend rates equal and this requires a conservative dividend policy. The share-holders should also realise that a conservative dividend policy may apparently be prejudicial to their interest in so far as they are not allowed to share in high profits. But really they are not losers but gainers. For, even in the bad years, it will be the policy of the concern to maintain the rate of dividend from the Dividend Equalisation Fund, even though no or very low profit is being earned. Besides, a stable dividend rate, by increasing the confidence of the share-holders in the particular scrip, facilitates capital appreciation, which is beneficial to all concerned with the concern, including the share-holders. Hence greater emphasis should be put on this aspect of the question.

CHAPTER XIII.

TRADE FINANCE IN INDIA.

Up to this time, we have devoted attention to one aspect of finance, *viz.*, producer's finance. Although the use of the words "corporate finance" also includes distributor's finance as well, yet in actual use of the words, we have meant only producer's finance and carried on with our discussions in that line. In the present chapter our sole purpose will be to discuss some aspects of trade finance as it is to be found in this country. The discussions on finance in this country have in the main centred round industrial or producer's finance. And although the aspect of finance known as trade finance or distributors' finance has found some place in treatises on banking, no separate treatment as such of the same has been made. The problem of trade finance needs discussion from two points of view—internal trade finance and external trade finance; and in so far as the agencies financing these two are in the main distinct and separate, we shall take up their study, in brief, in so far as our space permits, one by one.

I. Internal Trade Finance.

Among the agencies, financing the internal trade of India, mention may be made of merchants and commission agents as the principal source. In Indian terminology they are called *Arhatiyas* and are of two types, *Kuchcha* and *Pucca*. The *kuchcha Arhatiya* sometimes advances loans to village merchants and producers, generally on condition that they bring their produce to him and sell share either to or through him. As soon as the produce is sold and weighed over for the customer, the seller receives payment for the same; the *kachcha Arhatiya* may allow a few days before he receives payment from the purchaser. The practice in this respect varies. For, while in some markets the buyer is required to make payment on the same day, in others certain time limit varying from 3 days to about two weeks is allowed. In so far as the

kachcha Arhatiya's money is working during the gap between the payment to the seller and receipt from the customer at the end of the time limit granted, the *kachcha Arhatiya* may be said to occupy a place in the internal trade finance of India.

The *pucca Arhatiya* mainly works on behalf of the outstation buyers. He receives orders from them and keeps them informed regarding market conditions from time to time. At times the representative of the buyer visits the *pucca Arhatiya's* shop and makes purchases through him. The presence of the representative of the buyer is neither always possible nor at all times necessary. At times, however, particularly when the transaction is a new one, personal presence, of course, avoids a lot of trouble and at times, even after creating some confidence in the mind of the customer, the *Arhatiya* proves too shrewd. But this sort of happenings is few and the *Arhatiya* works for the customer during his absence, arranging for the purchase, pack, despatch, etc. At times however the *Arhatiya*, particularly when he happens to be the owner of a bigger firm, buys produce on his own account as well. The *pucca Arhatiya* usually has transactions with *kachcha Arhatiya* to whom he makes payment for produce purchased on behalf of his clients from whom he recovers the money later on with interest. When the party is a new one, the *pucca Arhatiya*, in order to safeguard his position, takes earnest money from the customer usually to the extent of one-fourth of the total value of purchases, this money being utilised both for meeting incidental expenses and as margin against a fall in prices. The rest of the money, usually 75 per cent. is advanced by the *Arhatiya*. The capital used by the *pucca Arhatiya* is usually his own, being supplemented from time to time by money obtained from relatives, friends, acquaintances and at times from banks. Sound firms of long standing have large sums deposited with them and it is actually found that in slack season they refuse deposits or accept them at no or a very nominal rate of interest. The *pucca Arhatiyas* also finance the internal movement of produce. Current accounts are maintained with the *Arhatiyas* by their clients at other markets and interest is paid on outstanding balance. Where goods are consigned to distant markets on their own account for commission sale by *Arhatiyas*, an advance of anything

between 70 and 85 per cent of the value is drawn against the consignment. This advance and the interest thereon are adjusted when the final accounts of the whole consignment are made out. Side by side with their business as merchant and commission agent, some of these *pucca Arhatiyas* have got banking functions like advancing loans, discounting hundis and bills of exchange, etc.

Immediately after merchants and commission agents who are by far the most important agency in financing inland trade of India, come the shroffs or indigenous bankers, advancing loans on the security of goods. They play a very important part in financing the internal trade of the country and belong mostly to the Marwari, Multani and Sindhi communities and are established in large number in practically all the chief markets of the country. When the *Arhatiyas* require funds, resort is usually taken to the indigenous banker, and not to the joint stock bank in the first instance. They are preferred to banks, because they have a personal contact with their clients, and because they transact business at odd hours on elastic terms and avoid certain formalities insisted upon by banks. The *pucca Arhatiyas* are financed by shroffs and indigenous bankers through the medium of promissory notes or *muddati hundis* or long term drafts or bills of exchange at varying rates of interest depending upon individual circumstances and money market conditions. When large amounts are involved, promissory note is used in order to save stamp duty. There is another and more important reason for which also promissory note is liked, viz., that since it is not a negotiable instrument, it entails little publicity, a factor which is much emphasized upon in Indian business. The rules regarding repayment are never strict. Those firms which can manage to get loans on promissory note do not use *hundi* in general. Some indigenous bankers who maintain link with the joint stock banks, and often take advances from them, do not however take promissory note in so far as it is not negotiable instrument and would therefore not be taken by the banks. On occasions loans are also granted against stocks of produce and in that case the procedure is the same as that followed by the joint-stock banks, less unnecessary formalities. The indigenous bankers also advance loans on personal security

and discount *hundis*. In recent years there has been a marked change in the activity of indigenous bankers and they are coming to combine trade with banking more and more. Some have explained this as being due to their preference to 'speculative' activity which is connected with trade; but the main reason is that their original business has been encroached upon by the gradual spread of banking system.

Whatever that may be, the shroff is inherent and unavoidable in the trade and commerce of the country. To-day, the shroffs and modern banks work side by side, and although the importance of the former has declined to some extent owing to the expansion of modern banking facilities, he still plays a much greater part in financing the internal trade of the country than the joint-stock banks. The reasons for this survival are many. In the first place, the indigenous banker is a product of the Indian soil and is therefore more adjusted to the economic system. Secondly, his business is facilitated because of close personal contact with and intimate knowledge of the family history of their clients, and details regarding their creditworthiness and business standing and reputation. This enables him to avoid many of the formalities so much emphasized upon by the modern banks to the disgust of their clients. This is not all. A more important factor, adding to his advantageous position, is that after making loans, he can constantly observe the behaviour of his clients and the manner in which money is utilised. But then the institution of indigenous banking has become old and therefore needs reconstruction if it is to survive for long in sound condition. It was pointed out by the *Indian Central Banking Enquiry Committee* that there is room for improving the efficiency and extent of the shroff's business. The main lines in which improvement is to be effected were suggested as follows by the *Committee*:

(1) Licensing of shroffs who agree to operate on purely banking business;

(2) Formation of associations to standardise business practice; and

(3) Provision for better discounting facilities and co-operation with joint stock banks.

Banks as a rule do not make any advances to cultivators

but loans are sometimes granted to merchants and commission agents on the security of goods stocked, under their own lock and key in their own godowns or in approved godowns belonging to the merchants themselves. A sum of money varying between 65 and 75 per cent of the current value of the produce is advanced. The funds are not withdrawn all at once but are placed to the credit of the borrower and may be drawn at his convenience. If prices rise and it is expected that the rise is not a short period phenomenon, the market value of goods increase and so also the borrowing power of the client to that extent. In the same way, if prices fall, the bank requires the borrower to refund as much of the original advances as may be essential for keeping the margin fixed by the bank intact. Goods thus stocked are in general insured against fire. Withdrawals of stocks are allowed against deposit of funds provided the margin between the total value of the produce pledged and the loans advanced do not fall below 25 per cent as a result of fluctuation in prices. Banks sometimes form a pool in order to keep the rate of interest high. But this is not too common a feature in this country. In addition to the provision of credit against the security of pledged stocks, the banks also buy and discount *hundis*, remit money by telegraphic transfer and provide accommodation necessary for the conduct of trade. Banks do not however advance loans against *muddati hundis*. Apart from these, the banks also finance approved merchants by allowing cash credit, the limit of which is fixed in each individual case after making due enquiries into the business standing and reputation, creditworthiness, etc., of the prospective client. The approved firms are then allowed to draw money from their bankers up to the credit limit on the basis of currency drafts (*muddati hundi*) or promissory notes. Such credit is not however enjoyed by every firm and a small concern may sometimes arrange to obtain advances from a bank through a larger firm who has an approved credit with the bank. The rate of interest in such loans is comparatively small in so far as these loans may be recalled at a short notice. Besides, the banks help in financing the movement of crop by remitting necessary funds to assist purchases and by discounting demand drafts and *hundis*.

The part played by co-operative societies in the supply of distributor's finance is meagre. The purely credit societies which constitute a major part of the movement are not directly concerned with the question of trade finance. This attitude of the co-operative societies is not at all encouraging. A much better solution can be found if the co-operative societies adopt a middle course between the indigenous banker on the one hand and commercial bank on the other. It should transact business more or less on the limits followed by commercial banks, but like indigenous banker it should avoid all unnecessary formalities which may be of inconvenience to the co-operators. This function should conveniently be combined with the existing function of the credit societies, so that the members would be able to realise better price by spreading their sales over a longer period. A notable development of co-operative movement in this field on a small scale is to be found in Behar and Orissa where grain *golas* have been organised. The primary purpose of these grain *golas* is to make loans of grain to members, particularly for seed purposes. Some of these *golas* are affiliated to Central Co-operative Banks, but most of them operate independently. Advances are in general made in kind though cash credit may also be given on a limited sale.

In some of the bigger markets, such as Amritsar and Hapur, the local Grain Trade Association or Grain Exchanges finance the storage of wheat out of sum which accumulate with them from margin money or deposits against future contracts. At times the funds offered are considerable. In so far as the management of the Grain Trade Associations is usually acquainted with the business standing and credit-worthiness of local traders, the investment of these idle funds does not involve too much of a risk. However, in so far as these funds can be available only to a limited number of persons of guaranteed business reputation, this source of finance can be regarded as extremely meagre.

Finally we must consider how the exporters provide themselves with funds in making purchases in inland centres. The exporters provide themselves with funds by selling sterling bills of exchange usually drawn at three months' sight or telegraphic transfers to exchange banks which handle foreign

exchange at various port headquarters of the firms in question. Another source of local funds arises from the sale proceeds of imported goods. Funds obtained in this way are utilised for purchasing indigenous products. Where receipts however exceed local requirements, the surplus funds are remitted to London by the purchase of sterling telegraphic transfers. The financing of up-country buying agencies has undergone much modification. Previously, for greater safety, currency notes, in halves, were often sent by registered post or messenger from the up-country headquarters of the shippers to some of the smaller sub-agencies or outstations, the second halves being forwarded only after acknowledgement of the receipt of the first halves. Specie in the form of silver used also to be sent to buying centres under escort; but since the spread of banking facilities and the increased circulation of coin and currency notes, these measures are rarely followed at present. At present up-country buying agencies are normally financed by the sale locally of the firm's *hundis* drawn on the port headquarters or funds may be remitted by telegraphic transfer through the Imperial Bank of India or other exchange banks. In some cases, *Arhatiyas* are authorised to finance upcountry agencies, the *Arhatiyas* being repaid by cheques or drafts. The exporters pay 70 to 80 per cent of the value of goods sold to them on presentation of the Railway Receipt and the accounts are finally cleared after the produce has been finally sampled and weighed at the agency or port according as the goods are purchased at the agency pass or port pass basis. Some of the big exporting firms advance loans on stocks of produce pledged, like banks, on similar conditions.

No less important is the inland remittance of funds for the internal trade finance. Remittances may be made by means of *Darshani Hundi*, bank draft or telegraphic transfer or by actually remitting cash under registered and insured cover. However, it is usually customary to send money by *darshani hundi* for the adjustment of trade accounts between different markets. The consignee may purchase a *darshani hundi* payable at the consignor's market, or as more often happens, the consignor may draw on the consignee and discount the *hundi* in his own market or with some local bank. Banks

usually make advances only against such *hundis* as are accompanied by Railway Receipts. It is usually customary for consignors to send the Railway Receipts for collection through a bank. The R/R is accompanied by a *darshani hundi* drawn on the consignee and it is only delivered to the latter when the *hundi* has been duly honoured by him. Where banking facility is not available or is not availed of, an alternative method of receiving payment for goods despatched is that the Railway receipt and the accompanying *hundi* are forwarded for collection to some reliable firm at destination. Where however the consignor is fully satisfied regarding the credit-worthiness of the consignee and/or the relation between the two parties is of long standing, the R/R may be sent direct to the latter. Where a small amount is involved, it is more convenient to avail of the device of mail order business of sending R/R per V. V. P. For goods consigned on commission sale, the usual custom is to draw on the consignee to the extent of 75 to 80 per cent of the invoice value and where goods are consigned to order, the full value of the goods is drawn.

II. *Financing of Coasting Trade of India.*

The coasting trade of India is not anything new. Any country having an extensive coast line is bound to develop this kind of trade. India is no exception. And although the volume and value of the coasting trade are much less when compared with her foreign trade as well as her inland trade, they are by no means negligible. Until recently this coasting trade as also the foreign trade became a virtual monopoly of non-Indian shipping companies. Yet in recent years, the Indians have, inspite of all obstacles placed in their way, have pushed forward in matters of coasting trade. The need for the reservation of coastal traffic for Indian shipping will be considered in the third volume of the present work. For the present we shall restrict ourselves to a discussion of financing of the coasting trade of India.

It is well-known that the coastal traffic to-day is being carried both by steam ships and sailing vessels. The introduction of steamship is but a recent innovation and the age-

long practice is to carry goods by sailing ships. Even to this day, the sailing ship has not been totally ousted from the competitive ground. It is true that steam ships have several advantages over the sailing vessels, but the latter also have certain advantages of their own over the steam ships which have enabled them to continue in the field. According to the estimate of the Sorley Committee, the total number of vessels of the sailing type in the west coast of India in 1941-42 was 4,768, the total tonnage being 206,721. According to K. B. Vaidya, the total number of vessels in 1943 increased to about 5,300.

So far as the coasting trade carried by steam ships is concerned, the financing is not either peculiar or different and all up-to-date banking and insurance facilities are available to them. But not so in case of the sailing vessel traffic, in which the old indigenous process of financing is followed even to this day. Of course, in old times the need for finance of coasting trade was very much limited, partly due to the dearth of banking houses with their branches and agencies and partly due to the peculiar nature of the trade in which barter was very much common, the merchant acting as the intermediary in the exchange of goods between two places. In any way, to such extent as financing of coasting trade was essential, those concerned had devised their own method. Broadly, there were two methods. In the first place, the financing was done through some banking houses with the aid of *hundies*. The purchaser would advise the seller to draw a *hundi* on him through a particular banking house or merchant engaged in banking business. The latter used to have branches or agents in the other centre, to whom the *hundi* was sent for presentation to the debtor. When the debtor honoured the *hundi*, the agent or the branch officer intimated his principal of the same and the transaction was closed between them by book entries. The principal who had debited the amount would pay the same to the creditor. The merchant or banking house used to get commission for this service. In case the *hundi* was dishonoured, the branch authority or the agent of the banking house in the other centre was instructed to take delivery of the goods and dispose them of at as best possible a price as it could and intimate

the principal of the same so that he would pay the sum to the sender. In the other case however the payment to the sender is already made by the banker, who, then, draws a *hundi* on the purchaser payable to the agent of the banker. The banker gets a commission for this service. In one case, the function is one of collection of the amount of the *hundi*, in the other case, however, the sum is advanced by the banker and it is recovered by him from the purchaser. In case the purchaser is unknown or not thoroughly known, the banker before agreeing to make advances, would demand a part or full value of the goods to be remitted to him by the purchaser. No such demand was made in case the party was thoroughly known. The second practice is of more recent origin, the first one being the only one prevalent in ancient times. During the years of second world war the situation has altered and organised banking has come forward, though to a limited extent, in financing coasting trade. When the credit of the parties in the deal is sufficient, the banks become ready to advance even full amount. In other cases, however, the banks come ready to discount the shipper's bill only when it is accompanied by the requisite insurance policy. Thus the organised banks also are gradually coming forward in the field.

III. *External Trade Finance.*

Before we take up the discussion on external trade finance in India, we shall devote some space—which is not altogether unnecessary—to external trade finance in other countries, in order to drive home the fact that the exporter as well as the importer in other countries is in much favoured position. The growing dissatisfaction of the Indian business community who handle foreign trade of the country to some extent, however negligible, became expressed before the *Indian Central Banking Enquiry Committee*. There was ample reason for that, and although nothing has as yet been done to remove the standing grievances, yet this expression has made it clear how much handicapped the Indian trading community is in matters of the foreign trade of their own country. The external trade finance has, broadly speaking, two

aspects—how debtors remit money and how creditors draw money, in brief, debtor's remittance and creditor's drawing. We shall take up these two one by one.

What is debtor's remittance? In the simplest case, the exporter sends the documents direct to the importer and it is for the latter to arrange for the remittance of money in accordance with the invoice value. If no arrangement has been made between them regarding the credit period, it is intended that the payment should be "sight" payment. This payment is known as Debtor's Remittance. But the next question is, how should the debtor remit the money? He can do it in various ways. He may get hold of the currency of the country to which payment is to be made and send it or he may send specie or even coins. But in actual practice this course would be exceptional in so far as the remittance of specie or coins not only involves great cost but also enormous risks. The debtor may take another course. The debtor in this country may have sums due to him by his debtors in the creditor's country which he can arrange to be paid to his creditor in the other country or there may be some reciprocal dealings between the two parties, both being debtor and creditor at one and the same time. In either case, the balance, after the accounts are adjusted, is to be paid. The debtor may remit the money (or the balance money) by purchasing bills of exchange on the creditor's country arising from his country's exports and sending them to his creditors who may realise the money from the debtors in their own country. But a perfect coincidence between the debt of the importer in this country and the value of the bill of exchange is a thing which it is too much to expect. The best method is therefore to seek the assistance of the bank who will issue their own draft on their correspondent in the creditor's country—provided, of course, the same bank has its branch or correspondent in the other country—for the amount of the debt. Apart from this, there are two other methods—telegraphic transfer and mail transfer. Telegraphic transfer is used when the parties are in a hurry to settle the account. In that case the debtor will arrange with his bank to cable the money either to the creditor direct or to his banker. In case the remittance is not extremely urgent and the parties not willing, to incur the

expenses of cabling the money, the debtor's bank will send Mail Transfer or Mail Payment Order, if necessary by Air Mail. The arrangement is that the debtor's bank sends a letter to their correspondent instructing him to pay the creditor the amount of the debt direct or through the latter's bank. So far we have discussed the case of sight payment. But sight payment is not very common. In most contracts it is agreed that the credit period is to be allowed and it commences from the date of the arrival of documents, and not from the arrival of goods, unless previously agreed.

It is clear that in case of debtor's remittance, a certain period of time is lost before payment is made, whether credit period is allowed or not. For, the period from the time of shipment of goods until eventual payment is one in which the seller is trusting his money to the buyer. This arrangement the seller may not like and he may prefer creditor's drawing, in which the seller draws a bill of exchange and hands it over, along with other documents, to the bank for collection of the value of the bill. The bills may be of two types according as they are surrendered on payment or on acceptance—D. P. and D. A. bills, as they are usually called. But, from the standpoint of the seller trouble arises when a bill is handed over to the banker for collection. For, in this case the exporter does not get the money all at once but has to wait for a remittance or a letter of advice from the drawee's centre before he gets his money. During this period his money will remain idle. If there is an agreement between the two parties, he can charge interest on this money; but that is not always the case. Hence the bank comes forward and either buys the bills or lends money against them. The bank will purchase the bill only when the party is known to the bank or the bank is assured of the credit-worthiness of the parties, in particular of the drawer. For, in case the drawer refuses to pay, the bank comes back to the exporter, who, as one of the signatories to the bill, agrees that the bill will be met. The banks discount clean bills only on rare occasions, when the parties are thoroughly known and their credit-worthiness perfectly assured. Therefore the banks prefer documentary bills where they have also the security of goods exported. When the transaction takes place in foreign currency, it is not known as

discount but as negotiation. In this case, when the bill is negotiated, the exporters get an amount according to the existing rate of exchange between the two currencies, after of course allowing a margin for any immediate change in exchange rate, cost of collection, discount of bills at foreign centre, and any other expenses.

Sometimes the bank advances money against the security of the bill. The exporter, in this case, gives the bank a letter of hypothecation, hands over the bill for collection and asks for accommodation against its security. It is not the practice with the banker to advance the full value of the bill; he always keeps a margin as safety and prepares a certain percentage of the value according to the nature of the transaction and those of the parties involved in the deal. Another type of credit, which is more often used when goods are shipped "on consignment" to some agent of the exporter, instead of to some foreign importer, is known as exporter's credit. The arrangement is like this. The exporter approaches the bank for accommodation in the form of acceptance credit and if the accommodation is allowed, the exporter draws bills on the bank according to his requirements, of course, within the limit of total amount outstanding which has been agreed upon and provided that the security offered covers bank acceptance after leaving a good margin for security. When the goods arrive in the country of import, they are stored in a warehouse under the control of the bank or its agent.

Let us now consider the question of trade finance from the standpoint of the importer. First of all, let us consider the case of banks acting as agents for foreign collections inwards. In this case, the bank inside the country of import may act as agent for foreign collections inwards. If the bill happens to be a D/P bill, some difficulty arises for the drawee in so far as he has to make payment before he gets hold of the documents of title. Therefore what is usually done is that the drawee requests the drawer to send the bill for collection through his banker, the collection being made through the bank of the drawee. Accordingly, the drawer when lodging the collection with his bank in foreign centre may stipulate that it is to be through a particular bank, being the bank of the drawee. The advantage of this arrangement is that since

the drawee's bank knows the financial standing of its client, it may violate the instructions, on its own responsibility, of course, and allow the drawee access to goods before the payment is made. From the standpoint of law, the drawee's bank secures its position by taking a Trust Receipt from him.

Another variety of credit used by importers is documentary credit. In its simplest form, the opening of credit can be done by the importer in his own books. The trade order that he has placed is regarded by the importer as a pledge of his own credit given to the exporter for providing for eventual payment and he sends a letter or cable to the exporter to the effect that he has accredited him for the amount in his accounts. When this type of documentary credit is opened, the practice most often is to send the letter or cable through the bank, in order to ensure the validity of the contract and to strengthen the legal claim of the exporter for the value of goods sent. A more complicated type of documentary credit is negotiation credit in which the buyer instructs his bank to arrange for the purchase of drafts drawn on him by a bank in the country of export. When this instruction is received, the importer's bank requests its own branch, if any, or its correspondent in the exporter's place to negotiate the bills on its client up to a certain amount; provided the bill is in order and accompanied by appropriate documents. Since the whole transaction takes place through banks or their correspondents, there is a greater degree of security, particularly for the bank or correspondent in the country of export. These bills are discounted at a less favourable trade bill rate. So far as discount rate is concerned, an improved type of credit is bank credit, in which the credit of the bank is substituted for the credit of the individual or firm or company importing goods. For, in this case, the exporter instructs the importer to open credit with some bank, under which the bill will be drawn on the bank and not on the importer. Since the bank figures important, the rate of discount is comparatively cheaper than that in documentary credit. The bank credit may be either revocable or irrevocable. In the former case the issuing bank can withdraw credit at any time without notice, which it cannot do in case of irrevocable one. It may however be asked that if, in case of revocable credit, it can be with-

drawn without notice, it will create enormous trouble for the importer, for he may only find, when goods are in transit, the credit revoked at the sweetwill of the bank. But it is more often resorted to because of the fact that in case of revocable credit, the bill is drawn, not on the importer, but on the bank and therefore it gets the best discount rate. And although it is revocable, it is not the underlying feature of any trade to put any party in difficulty, and the least in banking. At the same time the bank's position is more safe in so far as it can withdraw the facility in the event of malafides by the seller. Where a stream of purchases are concerned, a more convenient type of credit is running or revolving credit, which implies credit arranged through a particular correspondent of the importer's bank in the exporter's centre by which bills up to a certain amount are permitted to be outstanding at any one time. This variety of credit has the advantage that it saves the buyer and his bank the trouble of constantly opening new credits. When goods to the extent of the value of the maximum limit allowed have been exported, the credit is considered to be temporarily exhausted. When however the first bill is paid, and advice to that effect is received, a further bill can be negotiated and the process will go on in this way.

Now let us turn to conditions in India. When goods are exported from India, export bills are drawn by the exporter, usually for a currency of three months, against credit opened by the importers in other countries with London banks and finance houses and advised to India through the medium of exchange banks. The bills are drawn in sterling although for Japan and China they are drawn in yen and rupee respectively. The bills usually used in the export trade of the country are D/A bills which, as already noted, are usually for a currency of three months, the rate of interest on which being naturally higher than that for a demand bill. When an Indian exporter has drawn a bill, he takes it to an exchange bank and discounts it. The bills are scarcely given for collection, for, in that case the exporter will have to wait for a certain period before he receives payment. The banks, after receiving the bills, send these bills to London and present them for acceptance, and after endorsement by exchange banks in London, the bills are usually discounted in the open

market. This is done because the banks do not hold the bills till maturity unless of course the money market conditions are quite easy.

The export trade finance can be better understood if we take a concrete case, say, of oilseeds. As already noted, there are two types of shipper firms—those of Indian and those of non-Indian origins. The Indian export houses handle a negligible amount of transaction. They effect their sales through their representatives or brokers working at important continental ports. Before the Indian shipper gives an undertaking for shipment, he requires that his customer should open in his favour an irrevocable letter of credit through an exchange bank. This letter of credit not only facilitates discounting of bills, accompanied by shipping documents, with the said exchange bank, but also enables the Indian shipper, if he be in need of funds for effecting purchase, to obtain advance against shipment, by executing a deed thereby giving an undertaking that he would ship goods by a particular time and negotiate bills through the bank.

So far as foreign export houses are concerned, the exchange banks distinguish between three categories,—first, second and third classes—in accordance with their business standing and reputation. The exchange banks are prepared to buy clean bills from first class export houses. They also accommodate them in another way, *viz.*, by accepting a documentary or clean “House Paper”, which is nothing but a bill which is drawn by exporter on its Head Office or branch at the other end. The second class export houses receive the same sort of treatment as Indian shippers. Even the reputed Indian shipper cannot get the same sort of accommodation as a first class non-Indian shipper.

The firms in the third category—which contains many of the Indian firms who fail to get a letter of credit opened in their favour by the importer—are in the most inconvenient position. In this case, the exporter consigns his goods through the banker and is given an advance to the extent of 60 to 70 per cent of the market price of goods. No bill is drawn under this arrangement, the goods being stored and controlled by the banker's agent or branch at destination. There the goods are delivered only against payment and after

the goods are sold out, the accounts of the exporter in the bank are adjusted.

The import trade of India is financed in one of the two ways. A small portion is financed by what is called acceptance credit. A London exporter who is sufficiently known to some London bank and is allowed to draw on it will draw bills for his exports, get them accepted by the bank and then discount them in the London money market. This is an instance of the opening of acceptance credit by the banker of the exporter in the interest of the latter. Another type of acceptance credit is also to be found in which it is furnished in connection with export bills and is opened by the banker of the importer in favour of the exporter. In this case, "the accepting bank.....forwards the relative documents to its branch abroad for collection of the proceeds of the bills from the London exporting firm's foreign office in India and a remittance is sent to London at or before the maturity of the bill."

But the greater portion of the India's import trade is financed by 60 days' bills, usually on D/P terms, drawn on Indian importers. The importer authorises the bank to make advances to the exporter on presentation to the bank of the bills of exchange and complete shipping documents. But so far as the Indian importer is concerned, he has to pay interest on these bills, from the date of the bill to the approximate date of arrival of proceeds in London. These bills are not generally discounted in the London money market because the funds invested in them yield a higher rate of interest than can be secured in London on the proceeds that may be obtained by discounting them. That is why they are held by the banks till maturity when they send them to India for collection. The Indian importer has not only to pay higher rate of interest over the whole period till maturity; he has also to suffer the consequences of the bill being on D/P terms. For, before he makes payment he is not entitled to obtain goods. The shipping documents go to the banks with the bills and they hold the goods till they are delivered to the consignee or his agent. Previously the banks used to allow piecemeal delivery free but "they have practically stopped." If the consignee needs funds for taking delivery of goods, he is given

a loan against the security of the goods up to twelve months or even longer. Piecemeal clearance of goods is however allowed in cases in which the importing houses finance the merchants. Goods are usually stored in Port Trust warehouse and the delivery order is given by the importing firms.

It has been pointed out by the *Bombay Banking Enquiry Committee* that "the existence of Port Trust warehouses coupled with that of the well-organised system of credit given by exchange banks and importing houses has resulted in the adequate financing of trade in imported goods." But the evidences given by Indian importers to the *Central Banking Enquiry Committee* tells a different tale. Thus it was considered by the Indian Chamber of Commerce and several Indian witnesses that the financing of the foreign trade of India is from the Indian point of view in most unsatisfactory condition. As already noted, the Indian merchants who import from abroad cannot do so on D/A terms but have to do business on D/P terms only. The representatives of the exchange banks tried to repudiate the charges, first, on the ground that the practice followed by the exchange banks in releasing imported goods on trust receipts tantamount, in their opinion, to drawing bills on D/A terms and secondly that D/A terms are mostly arranged between the exporter abroad and importer in this country and that the reason for the present practice of drawing invariably on D/P terms is probably that importers are mostly people with limited means. It has been pointed out by the exchange banks that they cannot grant D/A terms without instructions from the exporter abroad. It has however been contended by the Indian importers that the lack of such D/A facilities is in some cases due to the unfavourable references given by the exchange banks, but the representatives of the latter have pointed out that bank references are not the sole basis of guidance to the exporter abroad who also tries to get into touch with the importer in India through a travelling agent, and unless he is thoroughly satisfied, he does not allow D/A terms. Whatever the reason, the fact that discrimination against Indian importers takes place cannot be denied. The much talked of "practice of releasing imported goods on trust receipts" is not equivalent to D/A terms, as it involves higher charges on account of loans

obtained on trust receipts. Another grievance brought to the notice of the *Central Banking Enquiry Committee* was that in order to get a confirmed letter of credit, even first class Indian importing firms are required to make a deposit of 10 to 15 per cent of the value of the goods with the exchange banks, while European houses in Calcutta are not required to make such deposits. The representatives of exchange banks pointed out that at least 9/10ths of the import business is done without credits at all and that the question of deposits in other cases really depends upon the standing of the importer and also to some extent on the nature of the commodities imported. Their contention is to some extent true. For, the greater part of the foreign trade of India is in non-Indian hands. Therefore in their case the question of taking deposits does not arise. The discrimination takes place against Indian concerns. The representatives of the exchange banks have explained this by stating that a large part of the import business is carried on without credits and that with regard to that part which is done with credits, no discrimination is done between Indian and non-Indian importers. Whatever the reason, in competition the Indian firms are at a disadvantage. Similarly complaint has been made that the banks do not generally discount the bills of Indian exporters without margins and securities; but this is not done in case of non-Indian firms. The representatives of the exchange banks have explained this by stating that in case of the latter arrangements exist at the other end which make it safe for the banks to pay full discounted value of the documentary bills. But still it must be admitted that the Indian firms are at disadvantage.

It was long ago pointed out by Keynes in his *Indian Currency and Exchange* that there is *prima facie* some danger to the stability of the Indian financial system in the fact that its money market is largely financed by funds raised not permanently, but for short periods, in a far distant foreign centre. It is, of course, true that Keynesian prophesy has not proved very much correct because of the fact that the exchange banks have been able to raise funds in India; but yet it is unfortunate that Indian banks have so far practically avoided foreign exchange business. According to the *Central Banking*

Enquiry Committee, the main reasons for this have been the competition of well-established non-Indian foreign exchange banks whose position is very much strong in respect of capital and reserve, non-existence of overseas branches of Indian banks, full occupation of the resources of Indian banks in internal business which is more profitable in character in comparison to foreign exchange business, etc. The weakness of Indian banks from the standpoint of capital and reserves and existence of branches overseas cannot be denied. But it is not proper to say that foreign exchange business is not sufficiently profit-earning, as is the experience of some Indian banks in this business, although to a very limited extent. But the real cause of non-participation is the lack of experience on the part of Indian banks and consequent unwillingness on their part to participate in this field of business. Another and a more important reason, as revealed from the working of the Tata Industrial Bank, is "that of obtaining sufficient import bills. A large portfolio of only export bills entails commensurate forward T. T. sales by way of cover, with the result that profits are partially curtailed."

Now let us study in brief how these foreign exchange banks carry on the transaction. The understanding of the operation requires a knowledge of the trade balance of the country. When exports from, and imports to, a country are balanced, no special problem arises, because the trade condition may be said to be balanced. But so far as India is concerned, in normal years, she has a favourable balance of trade, with the result that the proceeds of import bills received by the Indian branches of the exchange banks for collection are in most years, even when supplemented by considerable deposits that they obtain, insufficient to provide funds for the purchase of all the exporters' bills offered to them. The banks place themselves in funds by re-discounting their bills with the Imperial Bank of India and the Reserve Bank of India, by selling sterling drafts on London to the Reserve Bank; and by importing sovereigns and gold and silver bullion.

Prior to May, 1923, and to a certain extent up to March, 1925, the obligations of the Government of India in England in connection with Home charges, stores purchase, etc., used

to be met by the sale by the Secretary of State for India of Rupee bills of exchange, usually known as Council Bills, and telegraphic transfers payable at the Treasuries in India. But this was not the only objective behind the sale of Council Bills and telegraphic transfers (both together known as Council Drafts). For, at times the device was stopped in order to force up the exchange value of the rupee by a temporary cessation of the sale of Council Drafts. This had the effect of making rupee scarce and tended to raise the exchange value of rupee in terms of sterling, as was the case for some years after 1893. When in 1898 the exchange value of the rupee had sufficiently risen, an Act was passed authorising the sale of Council Drafts against gold set aside at the Bank of England as part of the Indian Paper Currency Reserve and notes of corresponding value were issued in India to meet Council Drafts. Among various other objectives behind the device, one very important objective was "that of securing the convenience of trade and that of so manipulating the disposition and location of the resources of the Government as to give the fullest effect to Government policy in matters of currency, exchange and finance." The device functions like this. Whenever there was a demand for remittance to India and money was wanted for any purpose by the Secretary of State, an announcement was made on each Wednesday as to the total amount for which Council Bills and telegraphic transfers were to be sold on next Wednesday. Tenders were invited from intending purchasers and allotments were made to the highest bidder, subject to a minimum price. On intermediate days, Intermediate or Special Bills were made available at a somewhat higher rate, the exact rate and minimum amount of such offers being fixed for the week on each Wednesday. This system of sale of Council Bills in England was replaced by that of purchase of sterling in India—to a certain extent since May, 1923, and entirely from March, 1925. In 1923-24, while the weekly sales of Council Bills continued as before, the sale of intermediaries at higher rates, was stopped and replaced by the purchase of sterling in India from banks and private financial houses willing to sell their sterling resources in London for rupees offered to them in India. These purchases were conducted by the Government through the agency

of the Imperial Bank. In 1924-25 the purchase of sterling became the principal method of remittance; the weekly sale of Council Bills was occasionally taken up when a steady and continuous demand for Council Bills manifested itself. During 1925-26, the old system was not at all used and its place was occupied by the system of sterling purchase. Too much was made of the new device by Sir Basil Blackett when he said that "our purchases of sterling have enabled us to ease the market in two ways. First of all the rupees we paid out for purchases of sterling, were available for the banks and others for the purpose of re-lending.....In addition, in order to put the Government of India in funds with which to purchase sterling and also to increase the amount of currency available for general trade purposes in India, the Government of India have to the extent of Rs. 6 crores already added to the amount of currency in India by transferring money from the Secretary of State's balances to the Paper Currency Reserve in London and issuing rupees against it." The Hilton Young Commission recommended the purchase of sterling by competitive public tender and the publication of the weekly returns of remittances. Accordingly, since April, 1927, the system of purchase in India by public tender has been inaugurated. The Government of India meet their sterling obligations by the purchase of Sterling Drafts on London, for immediate delivery, by weekly auction on Wednesdays at Calcutta, Bombay, Madras and Karachi. Only approved banks and firms can tender at these auctions and allotments are made upto the amount put up to tender. Sterling drafts are also purchased on days other than Wednesday. Ordinarily most of the amounts offered for sale come from the exchange banks.

With the establishment of the Reserve Bank of India, the responsibility of providing funds for the Government of India's expenditure in England has been placed on the Bank and the Government of India do not now purchase sterling in the market, but obtain their requirements from the Bank. From April, 1935, onwards, the Reserve Bank of India has been placing itself in funds, to meet this responsibility, by the purchases made only from the banks named in Schedule II graph as well as at Delhi, on the same lines as before except

that the purchases are made only from the banks named in Schedule II to the Reserve Bank of India Act and are subject to a minimum limit of £75,000 in each case. The system has enabled the Reserve Bank of India "to take advantage of a firm or rising exchange and also to prevent the appreciation of the rupee above the point fixed by the Reserve Bank of India Act. The object underlying the new system is that the factors influencing the immediate course of exchange can be much more accurately and promptly judged in India and the purchases can be regulated much more satisfactorily with reference to the varying conditions of the market.....This method suits the exchange banks very well, as they can sell sterling to the Reserve Bank of India against their London balances, which are increased by their purchases of export bills in India, and thus immediately replenish their funds in this country."

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